CLERK'S COPY.

TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1942

No. 24

MARINE HARBOR PROPERTIES, INC.,
PETITIONER,

vs.

MANUFACTURER'S TRUST COMPANY (SUCCESSOR BY MERGER TO THE MORTGAGE CORPORATION OF NEW YORK), AS TRUSTEE, ETC., ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR CERTIORARI FILED FEBRUARY 13, 1942.

CERTIORARI GRANTED MARCH 16, 1942.

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United States Circuit Court of Appeals

FOR THE SECOND CIRCUIT.

1

IN THE MATTER
of
MARINE HARBOR PROPERTIES, INC.,
Debtor-Appellee,

MANUFACTURERS TRUST COMPANY (successor by merger to The Mortgage Corporation of New York), as Trustee for the benefit of certificate holders in mortgage guaranteed by Bond and Mortgage Guarantee Company, Guarantee No. 181,568,
Petitioner-Appellant,

MAURICE RUBINGER, Trustee of Marine Harbor Properties, Inc., SAMUEL SILVERMAN, additional Trustee of Marine Harbor Properties, Inc., and MORTIMER RUBENSTEIN, Foreclosure Receiver, 2
Appellees.

Statement Under Rule XIII

The name of the court and the title of the case is as follows: United States District Court, Southern District of New York. In the Matter of MARINE HARBOR PROPERTIES, INC., Debtor, in a proceeding for the reorganization of a corporation No. 79,473.

Marine Harbor Properties, Inc., filed its petition for reorganization, pursuant to Chapter X of the Chandler Act, on the 17th day of September, 1941, praying "that the court 3
find that the petition complies with and is properly filed under Chapter X of the Bankruptcy Act; that the debtor is unable to meet its debts as they mature; that said petition has been filed in good faith", etc. Thereafter, an order was signed by Hon. John Bright, *D.J.*, on September 17, 1941, approving the debtor's said petition. Neither the presentation of the petition nor the presentation or entry of the order of September 17, 1941, was on notice to The Mortgage Corporation of New York.

An order to show cause was obtained by The Mortgage Corporation of New York, as Trustee, on September 27, 1941, for an order vacating the order of September 17, 1941 which had approved the debtor's petition and appointed Trustees

of the debtor's estate, and dismissing said petition. A hearing was held before Hon. John Bright, *D.J.*, upon said order to show cause, and the application was denied in all respects with an opinion and an order was entered thereon by Hon. John Bright, *D.J.*, dated October 3, 1941.

The Mortgage Corporation of New York was merged into the Manufacturers Trust Company pursuant to agreement of merger under Section 441 of the New York Insurance Law, as of September 30, 1941.

The notice of appeal was duly filed with the clerk of the court on the 3rd day of October, 1941. The undertaking on
5 appeal was duly filed with the clerk of the court on the 3rd day of October, 1941.

FRIEDLAND & FRIEDLAND, Esqs., are the attorneys for the debtor-appellee and they have their offices at 291 Broadway, in the Borough of Manhattan, City and State of New York.

HUGHES, HUBBARD & EWING, Esqs., are the attorneys for the appellant MANUFACTURERS TRUST COMPANY, formerly The Mortgage Corporation of New York, as Trustee for the benefit of the holders of certificates in the first mortgage covering the premises owned by the debtor, and they have their offices at 1 Wall Street, in the Borough of Manhattan, City and State of New York.

6 MAURICE RUBINGER, Esq., is one of the Trustees under the order of the District Court and has his office at 160 Broadway, in the Borough of Manhattan, City and State of New York.

SAMUEL SILVERMAN, Esq., is one of the Trustees under the order of the District Court and has his office at 50 Broad Street, in the Borough of Manhattan, City and State of New York.

GEORGE ROSLING, Esq., is attorney for MORTIMER RUBENSTEIN, as Receiver, in the New York State Supreme Court, and has his office at 50 Court Street, in the Borough of Brooklyn, City and State of New York.

Notice has been given to the SECURITIES AND EXCHANGE COMMISSION which has its office at 120 Broadway, in the Borough of Manhattan, City and State of New York.

Notice of Appeal

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

IN THE MATTER

of

MARINE HARBOR PROPERTIES, INC.,

Debtor.

SIRS:

NOTICE IS HEREBY GIVEN that Manufacturers Trust Company, formerly The Mortgage Corporation of New York, as Trustee, Petitioner herein, hereby appeals to the United States Circuit Court of Appeals for the Second Circuit from the order of this Court dated October 3, 1941, made by Hon. John Bright, District Judge, wherein the petition of The Mortgage Corporation of New York, as Trustee, was, in all respects, denied and from each and every part thereof.

Dated, New York, N. Y.
October 3, 1941.

Yours, etc.

HUGHES, HUBBARD & EWING
Attorneys for Manufacturers Trust Company, formerly The Mortgage Corporation of New York
One Wall Street
New York, New York

10 *Order Appealed From*

To:

FRIEDLAND & FRIEDLAND
Attorneys for Debtor
291 Broadway
New York, New York

MAURICE RUBINGER, Esq.,
Trustee
160 Broadway
New York, New York

SAMUEL SILVERMAN, Esq.,
11 Trustee
50 Broad Street
New York, New York

SECURITIES & EXCHANGE COMMISSION
120 Broadway
New York, New York

GEORGE ROSLING, Esq.,
Attorney for Mortimer Rubinstein, as Receiver
50 Court Street
Brooklyn, New York

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12 **Order Appealed From**

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE]

An application having been made by The Mortgage Corporation of New York as Trustee of a certain mortgage covering real property of the above-named debtor, for an order dismissing debtor's petition herein verified September

15, 1941 and vacating the order of this Court herein dated September 17, 1941,

Now, on reading and filing the order to show cause of this Court dated September 27, 1941, the petition of The Mortgage Corporation of New York as Trustee verified September 27, 1941, with the exhibits thereto annexed, the affidavit of Curtiss Ely Frank sworn to September 29, 1941, the affidavit of Joseph L. Long sworn to September 29, 1941, and the order of this Court dated September 24, 1941, in support of the motion and the affidavit of Gussie Hammer sworn to September 29, 1941, and affidavit of Samuel Silverman in opposition thereto, and said application having duly 14
come on to be heard on September 29, 1941, and after hearing Hughes, Hubbard & Ewing (Curtiss Ely Frank, Esq., of counsel), attorneys for The Mortgage Corporation of New York as Trustee, in support of said application, and Friedland & Friedland (Arthur S. Friedland, Esq., of counsel), attorneys for the debtor, in opposition, and Samuel Silverman, Esq., and Maurice Rubinger, Esq., trustees of the debtor, appearing and not opposing, and George Rosling, Esq., attorney for Mortimer Rubenstein as receiver, appearing but not opposing; and due deliberation having been had thereon, and upon reading and filing the opinion of the Court, it is 15

ORDERED that the application of The Mortgage Corporation of New York as Trustee be and the same hereby is in all respects denied; and further

ORDERED that the turning over to the trustees in bankruptcy by Mortimer Rubenstein of such moneys as he has in his possession as receiver in the New York State Supreme Court foreclosure action of the debtor's mortgage and his subsequent accounting shall be without prejudice to his application for receivership commissions and attorney's fees.

Dated: October 3rd, 1941.

JOHN BRIGHT,
U. S. D. J.

Order to Show Cause of Hon. John Bright dated September 27, 1941

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE]

On the annexed petition of The Mortgage Corporation of New York, as trustee under a declaration of trust dated December 12, 1938, for the holders of investments in certain premises covering 351-363 Marine Avenue, Borough of Brooklyn, County of Kings, City and State of New York, verified on September 26, 1941, and the Exhibits annexed thereto, and upon all proceedings had herein.

Let the debtor show cause before one of the judges of the United States District Court for the Southern District of New York on the 1st day of October, 1941, at 10:30 o'clock in the forenoon of that day or as soon thereafter as counsel can be heard in Room 506 in the United States Court House, Foley Square, City of New York, why an order should not be made and entered herein vacating the order of this Court herein dated September 17, 1941, dismissing the debtor's petition, verified September 15, 1941 and for such other and further relief as to the court may seem just and equitable, and it is

ORDERED that service of this order is to be executed on or before 12 P. M. of September 29, 1941, by delivering to and leaving a copy of the same with Messrs. Freidland & Freidland, attorneys for the debtor, 291 Broadway, Borough of Manhattan, City of New York, Maurice Rubinger, Esq., trustee, 160 Broadway, Borough of Manhattan, City of New York, Samuel Silverman, Esq., additional trustee, 50 Broad Street, Borough of Manhattan, City of New York and George Rosling, Esq., 50 Court Street, Borough of Brooklyn, City of New York, attorney for Mortimer Rubenstein as Receiver, and it is further

Dated, September 27, 1941.

JOHN BRIGHT
U. S. D. J.

19

Petition of The Mortgage Corporation of New York, as Trustee, to Vacate Order Approving Petition and to Dismiss Debtor's Petition

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE]

20

To: The Honorable Judges of the United States District Court, Southern District of New York.

The petition of The Mortgage Corporation of New York as Trustee respectfully shows to the Court as follows:

1. The Mortgage Corporation of New York, a domestic corporation duly organized and existing under the Insurance Law of the State of New York, is trustee under a declaration of trust dated December 12, 1938, for the benefit of the holders of mortgage investments therein, of a certain mortgage covering premises 351-363 Marine Avenue, Borough of Brooklyn, County of Kings, City and State of New York.

21

The premises covered by such mortgage are the same premises now owned by the debtor herein and described by the debtor in its petition as its sole asset. These premises for the sake of brevity will be hereinafter in this petition referred to as "the Mortgaged Premises".

The aforesaid declaration of trust was executed pursuant to an order of the Supreme Court of the State of New York, County of Kings, entered on December 6, 1938 pursuant to a plan of readjustment, etc. of the rights of the holders of investments in such mortgage. Copies of such declaration of trust, plan of readjustment, etc., interlocutory order and

22 *Petition of The Mortgage Corporation of New York, as Trustee, to Vacate Order Approving Petition and to Dismiss Debtor's Petition*

final order approving such plan are annexed hereto, made a part hereof and marked Exhibits A, B, C and D respectfully.

HISTORICAL BACKGROUND OF THE MORTGAGE

2. On or about April 28, 1931 Marine Building Corporation, upon information and belief the then owner of Mortgaged Premises, delivered its bond in the principal amount of $370,000 to Title Guarantee & Trust Company and secured
23 the same with a mortgage to Title Guarantee & Trust Company upon the Mortgaged Premises in like amount. This mortgage was recorded in the office of the Register of the County of Kings on April 28, 1941 in Liber 7634 of Mortgages, page 128 and indexed under Block 6126.

Thereafter Title Guarantee & Trust Company sold participation certificates in said bond and mortgage to the general public, which certificates were guaranteed by Bond and Mortgage Guarantee Company under its guarantee number 181,568.

Upon information and belief, thereafter Marine Building Corporation conveyed the Mortgaged Premises to Marine Holding Corporation and on or about February 15, 1933
24 Marine Holding Corporati.. conveyed the Mortgaged Premises to Marine Harbor Properties, Inc., the debtor herein, by deed dated February 15, 1933 and recorded in the office of the Register of the County of Kings in Liber 5324 of Conveyances page 108.

REORGANIZATION OF THE MORTGAGE IN THE STATE COURT

3. Pursuant to an order of the Supreme Court, County of Kings, dated August 2, 1933 and entered in the office of the Clerk of the County of Kings on August 3, 1933, George S. Van Schaick, Superintendent of Insurance of the State of

Petition of The Mortgage Corporation of New York, as Trustee, to Vacate Order Approving Petition and to Dismiss Debtor's Petition

New York, duly entered into the possession of the property and the conduct of the business and the rehabilitation of the Bond and Mortgage Guarantee Company, the guarantor of the above mentioned certificates of interest in said bond and mortgage.

Pursuant to powers granted to him as such rehabilitator under Sections 3 and 4 of Chapter 745 of the Laws of 1933 as amended (commonly known as the Schackno Act), George S. Van Schaick, Superintendent of Insurance of the State of New York, as such rehabilitator promulgated a plan for the readjustment, modification or reorganization of the rights of the holders of investments in the mortgage covering the Mortgaged Premises. Such plan contemplated the extension of the maturity date of the mortgage and the reduction of the rate of interest thereof. A copy of such plan is annexed hereto, made a part hereof and marked Exhibit E.

Notice of such plan was given, among others, to Marine Harbor Properties, Inc., the debtor herein as the then owner of the Mortgaged Premises.

Such plan came on to be heard before an Additional Special Term of the Supreme Court, County of Kings on October 24, 1934, at which time the debtor appeared by its then President, Abraham Hammer, and agreed in open court to the plan as promulgated by the Superintendent of Insurance and as amended by the court.

On November 24, 1934, the Supreme Court, County of Kings entered an interlocutory order approving the plan as proposed by the Superintendent of Insurance, amended by the court, and agreed to by the debtor and providing that the final order should be entered declaring the plan to be binding upon all parties thereto when 66⅔% of the holders in principal amount of the investments in such mortgage had approved the plan as amended: A copy of such interlocutory

28 *Petition of The Mortgage Corporation of New York, as Trustee, to Vacate Order Approving Petition and to Dismiss Debtor's Petition*

order is annexed hereto, made a part hereof and marked Exhibit F.

On December 6, 1934 the Supreme Court, Kings County, entered a final order declaring that 66⅔% of the holders in principal amount of mortgage investments had consented to the plan and that the plan was binding upon all parties in interest. A copy of such final order is annexed hereto, made a part hereof and marked Exhibit G.

29 The plan as finally approved by the court and agreed to by the debtor herein provided, among other things, as follows:

A. That the Mortgage be extended three years until December 1, 1937.

B. That the owner of the Mortgaged Premises pay interest on the unpaid principal amount of the mortgage at the rate of 6% per annum to December 31, 1934 and at the rate of 5% per annum to December 1, 1937.

On March 11, 1935 Title Guarantee & Trust Company, being the then holder of record of said bond and mortgage, entered into an extension agreement with the debtor, Marine
30 Harbor Properties, Inc., extending the payment of the bond and mortgage in pursuance of the provisions of the said plan of readjustment as amended, as agreed to by the owner and approved by the Supreme Court, County of Kings. A copy of such extension agreement is annexed hereto, made a part hereof and marked Exhibit G-1.

DESIGNATION OF THE MORTGAGE CORPORATION OF NEW YORK, AS TRUSTEE

4. The Legislature of the State of New York, by Chapter 19 of the Laws of 1935 (commonly known as the Mortgage

Commission Act), provided for the establishment of a Mortgage Commission of the State of New York and vested in such Commission all the powers previously vested in the Superintendent of Insurance of the State of New York by Chapter 745 of the Laws of 1933 as amended. These powers included power to promulgate a plan of further readjustment of the rights of the holders of investments in certificated mortgages to the extent of the appointment of a trustee of the bond and mortgage under a Declaration of Trust in a form to be approved by the Court.

In pursuance of these powers on June 1, 1938, the Mortgage Commission of the State of New York promulgated a plan to modify the original plan (Exhibit B hereto) to the extent of appointing a trustee of the bond and mortgage under an approved form of Declaration of Trust. Notice of a hearing upon such plan was given, among others, to Marine Harbor Properties, Inc., the debtor herein, as owner of the Mortgaged Premises and this plan was brought on before the Supreme Court, Kings County, in the same proceedings as the original plan.

After a hearing upon such plan on June 27, 1938, the Supreme Court, County of Kings, entered an interlocutory order approving the form of Declaration of Trust, appointing The Mortgage Corporation of New York as trustee, and directing that upon the consent to such plan by 66⅔% in principal amount of the holders of mortgage investments in said mortgage that a final order be entered declaring the plan binding upon all parties in interest. A copy of such interlocutory order is annexed hereto as Exhibit C.

On December 6, 1938, a final order approving the plan and designating The Mortgage Corporation of New York as trustee was entered by the Supreme Court, County of

Kings. A copy of such final order is annexed hereto and marked Exhibit D.

Such final order provides in part as follows:

> "ORDERED that this Court, having assumed jurisdiction of this proceeding, shall retain jurisdiction hereof until the complete liquidation of the Trust Estate and the termination of the trust; and the Trustee, or any other interested party herein, may apply at the foot of this Final Order upon such notice as the Court may direct for such other and further relief as to the Court may seem just and proper."

On December 12, 1938, The Mortgage Corporation of New York, duly executed the Declaration of Trust in the form approved by the aforesaid final order of the Supreme Court, County of Kings. Thereafter, pursuant to said final order the Title Guarantee & Trust Company and the Mortgage Commission of the State of New York assigned to The Mortgage Corporation of New York, as trustee, the bond and mortgage, including the extension agreement, covering the Mortgaged Premises.

FORECLOSURE PROCEEDINGS IN THE STATE COURT

5. On May 1, 1941 The Mortgage Corporation of New York, as trustee, commenced proceedings in the Supreme Court, County of Kings, to foreclose the mortgage on the Mortgaged Premises for the following defaults in the payment of interest and taxes:

> The sum of $9,250, being interest payable April 1, 1941;

Real estate tax due April 1, 1941 in the sum of $5,681, plus penalties to May 1, 1941.

A lis pendens was filed on May 1, 1941 (a copy of which is annexed hereto, made a part hereof and marked Exhibit H) and copies of the summons and complaint (copies of which are annexed hereto, made a part hereof and marked Exhibit I) were served the same day upon the defendants, Louis H. Pink, Superintendent of Insurance of the State of New York and Morris S. Tremaine, Comptroller of the State of New York. The debtor herein as owner of the Mortgaged Premises appeared generally in the foreclosure action by notice of appearance dated May 27, 1941.

On an affidavit, sworn to May 3, 1941, requesting the appointment of a receiver pending the foreclosure action, an order was granted on May 5, 1941 by Hon. Algeron I. Nova of the Supreme Court, County of Kings, appointing Mortimer Rubinstein of 50 Court Street, Brooklyn, New York, as Receiver of rents and profits of the Mortgaged Premises. A copy of such order is annexed to this petition, made a part hereof and marked Exhibit J.

Thereafter and on or about May 6, 1941 Mr. Rubinstein qualified as such Receiver and has been in possession of the Mortgaged Premises since that date and has managed the same in accordance with the terms of the order of his appointment.

NEGOTIATIONS FOR THE FURTHER REORGANIZATION OF THE MORTGAGE

6. Under Article III of the Declaration of Trust (Exhibit A) petitioner as trustee may not extend or otherwise modify the mortgage without first obtaining the approval

of the Supreme Court, County of Kings, by application in the pending reorganization proceedings. The final order approving the appointment of petitioner as trustee (Exhibit D) provides the machinery for such an application. The pertinent portion of that order is quoted on page 6 of this petition.

Petitioner has therefore on numerous occasions discussed with representatives of the debtor corporation a further modification of the mortgage. It was hoped that as a result of these conferences a satisfactory plan might be agreed upon, which plan petitioner could submit for the approval of the Supreme Court, Kings County in the pending reorganization proceedings, pursuant to Article III of the Declaration of Trust. The debtor made two concrete offers which petitioner submitted to its Trust Committee.

The first offer on October 11, 1940 provided for an extension of five (5) years with interest at the rate of 4% and amortization of 2% per annum. This proposal the petitioner's Trust Committee declined, feeling that the only fair plan under the circumstances would be one providing for 4½% interest and 2% amortization.

The debtor's second proposal was submitted to the Trust Committee on August 11, 1941 and contemplated a five (5) year extension with interest at 4½% and amortization of 1½%. This proposal the Committee again turned down, feeling as before that the only fair plan was the one indicated.

After the commencement of the foreclosure action, petitioner made it a requirement to any plan for further reorganization of the mortgage that the arrears of taxes and interest be paid in full so that the foreclosure action might be discontinued prior to application to the Court.

Petition of The Mortgage Corporation of New York, as Trustee, to Vacate Order Approving Petition and to Dismiss Debtor's Petition 43

PRESENT STATUS OF THE MORTGAGE

7. At the present time there are the following arrears upon the mortgage:

Principal due December 1, 1937	$370,000.00
Interest due April 1, 1941	9,250.00
Real estate taxes due April 1, 1941	5,681.00
Instalment of assessment due June 1, 1941	9.93
Total	$384,940.93

44

On October 1, 1941, next Wednesday, the following additional sums will be due:

Interest October 1, 1941	$ 9,250.00
Real estate taxes October 1, 1941 (1st half 1941-1942)	5,724.00

As a result, on October 1, 1941, there will be due upon the mortgage the total amount of $399,814.93.

As indicated above, Mortimer Rubinstein, as Receiver, has been in possession of the Mortgaged Premises since May 6, 1941. During the period of his receivership, based upon figures submitted by him to petitioner, he has made 45 the following rent collections:

Month	*Income*	*Expense Disbursements*
April	$ 204.	
May	3,055.	$708.65
June	4,824.	595.79
July	4,755.	595.56
August	4,819.	611.28
September	410.	
October	189.	

Petition of The Mortgage Corporation of New York, as Trustee, to Vacate Order Approving Petition and to Dismiss Debtor's Petition

Receiver now has on hand $8,580.37 with unpaid bills of approximately $750. All these figures are, of course, without deductions for Receiver's commissions or legal expenses.

Based upon his experience in operating the property, the Receiver has estimated to petitioner the following income from the property:

Collectible rent			$57,000.00
Expenses			
Salary	$7,200.00		
Coal	4,800.00		
Electrictiy	1,200.00		
Painting	1,800.00		
Elevator	600.00		
Refrigerators	1,200.00		
Management	2,280.00		
Ranges	600.00	$19,680	
Fixed charges			
Taxes	$11,000.00		
Water	1,100.00		
Insurance	1,200.00	13,300	
Total expenses			$32,980.00
Net income			$24,020.00

Based on this estimate, the property earns interest on the first mortgage of about 6⅔%.

When the Receiver took possession of the property, he advised petitioner that it was in a poor, run down condition. He estimates that the following repairs must be made to put the building in proper condition:

Petition of The Mortgage Corporation of New York, as Trustee, to Vacate Order Approving Petition and to Dismiss Debtor's Petition

Paint the halls	$ 900.00
Paint fire escapes	450.00
Paint window trim and putty	1,200.00
Repair the roof	1,000.00
	$3,550.00

The affidavit of J. L. Long (annexed hereto, made a part hereof and marked Exhibit K) a qualified real estate appraiser employed by The Mortgage Corporation of New York, indicates the value of the Mortgaged Premises to be:

Land	$65,000.00
Building	285,000.00
	$350,000.00

or $49,000 less than the amount which will be due upon the bond and mortgage on October 1, 1941.

From the foregoing and from the petition filed by the debtor herein, petitioner respectfully submits that debtor's petition was not filed in good faith within the meaning of Section 146, Chapter X of the Bankruptcy Act.

The admitted sole asset of the debtor is the Mortgaged Premises which is covered by the $370,000 first mortgage held by petitioner as trustee.

In a reorganization proceeding under state statutes the Supreme Court, Kings County approved a reorganization of said mortgage to which debtor agreed.

In these same reorganization proceedings The Mortgage Corporation of New York was appointed trustee of said mortgage. By its order appointing petitioner as trustee (Exhibit D) the State Court expressly retains jurisdiction of

Petition of The Mortgage Corporation of New York, as Trustee, to Vacate Order Approving Petition and to Dismiss Debtor's Petition

the proceeding until the complete liquidation of the trust estate (See Exhibit D, page 8) and provides that the "Trustee" or any other intereseted party may apply in the proceeding for further relief. Under this provision of said order petitioner may apply for approval of the further modification of the mortgage.

The Mortgage Corporation of New York as trustee for certificate holders has been in continuous possession of the bond and mortgage since December 12, 1938 under the direction and control of the Supreme Court of the State of New York. As such trustee petitioner is required to file a detailed annual accounting of its operations. Such accounts are judicially approved pursuant to statutory procedure by the Supreme Court, Kings County upon notice to certificate holders and others concerned.

The pending reorganization is but one of the many similar mortgage reorganizations before the State Courts under the machinery enacted by the Legislature of New York. This legislation was enacted for the protection of certificate holders and owners of real property subject to certificated mortgages following the collapse of the mortgage guarantee companies in 1933 and the depression in real estate values. As appears from the body of the petition, subsequent legislation was passed in 1935 (the Mortgage Commission Act) which sought to provide more adequate machinery in the light of two years of extensive reorganization experience. It was in pursuance of this latter act that petitioner was appointed as trustee.

The reorganization affecting this particular mortgage is pending before Mr. Justice George E. Brower in Special Term, Part VII of the Supreme Court, County of Kings. Mr. Justice Brower was designated by the Appellate Division

55

of the Supreme Court in 1934 to hear and pass upon such reorganization proceedings. Over a period of the last seven years millions of dollars in principal amount of mortgages, similar to the mortgage covering the Mortgaged Premises herein, have been reorganized in proceedings before him, and with the experience gained from these many proceedings of this nature, Mr. Justice Brower has been able to deal with these matters expeditiously and for the protection of certificate holders and property owners alike.

56

It is respectfully submitted therefore that in the pending State Court proceeding the rights of the certificate holders and debtor alike are being efficiently and fully protected and that to withdraw this mortgage from the pending State Court proceedings would not serve the best interests of the certificate holders therein.

In addition to the pending reorganization proceedings, petitioner, four months prior to the institution of the proceedings herein, commenced a foreclosure of the mortgage. A State Court Receiver has been appointed and has been in continuous possession of the Mortgaged Premises since May 6, 1941.

57

Petitioner believes that the State Court Receiver has been running the property in an efficient manner and collecting therefrom the maximum of rents obtainable.

It is respectfully submitted that to transfer the Mortgaged Premises from the State Court Receiver to a trustee in bankruptcy at this time would not serve the best interests of the certificate holders, since it would involve a change of operations at a critical time in the year and a duplication of expenses.

No plan of reorganization has been presented by the debtor and from the facts now before the Court, it is respectfully submitted that no feasible plan can be worked out.

58 *Petition of The Mortgage Corporation of New York, as Trustee, to Vacate Order Approving Petition and to Dismiss Debtor's Petition*

The appraised value of the property (See Exhibit M [K.]) is $49,000 less than the present indebtedness upon the first mortgage alone. It is difficult, therefore, to see how the debtor can have any equity in the Mortgaged Premises.

Any reorganization should, in the opinion of petitioner, involve a substantial reduction of the principal of the mortgage in view of the present "top heavy" nature of the mortgage.

59 As previously indicated, two plans have already been submitted by the debtor to petitioner, both of which petitioner's Trust Committee, after due consideration, felt could not be recommended to the State Court in view of the inadequacy of the provisions. Petitioner has been and is now willing to recommend to the State Court that the mortgage be extended for five years and the interest reduced to 4½% per annum, if the debtor will pay 2% in reduction of principal each year. This plan the debtor has been unwilling to meet, despite the apparent earnings from the property.

In the pending reorganization proceedings in the State Court certificate holders consented to the designation of petitioner as trustee. The effect of such designation, as indicated
60 by the terms of the declaration of trust (Exhibit A) was to vest in petitioner as trustee "all the rights and powers of an absolute owner" which includes the right to extend or otherwise modify the bond and mortgage. This power is limited in one respect. Article III of the Declaration of Trust provides that the petitioner as trustee may so extend or modify only with the approval of the Supreme Court, Kings County.

WHEREFORE, petitioner prays for an order directing the debtor and the trustees appointed by the order of this Court dated September 17, 1941 to show cause why the order herein dated September 17, 1941, approving the debtor's petition,

Petition of The Mortgage Corporation of New York, as Trustee, to Vacate Order Approving Petition and to Dismiss Debtor's Petition. 61

should not be vacated and the debtor's petition dismissed and for such other and further relief as to the Court may seem just and equitable.

Petitioner is requesting that this matter be brought on by order to show cause in view of the fact that the time for the Receiver to comply with the directions contained in the order of this Court of September 17, 1941 expires on Monday, September 29, 1941.

No previous application has been made to this Court or any other court or judge for the relief requested herein. 62

Respectfully submitted,

THE MORTGAGE CORPORATION OF NEW YORK

By JOHN W. REYCRAFT.
Vice-President

UNITED STATES OF AMERICA
STATE OF NEW YORK } ss.:
COUNTY OF NEW YORK

JOHN W. REYCRAFT, being duly sworn, deposes and says that he has read the foregoing petition and knows the contents thereof and that the same is true to the best of his knowledge and belief. 63

JOHN W. REYCRAFT

Sworn to before me this
27th day of September, 1941

SAMUEL E. ZALOUM

SAMUEL E. ZALOUM
Notary Public, Kings Co.
N. Y. Co. Clerk's No. 27
N. Y. Co. Reg. 3-Z-19
Commission expires March 30, 1943.

64 EXHIBIT A, ANNEXED TO PETITION

Original filed in Kings
County Clerk's Office on 12/28/38
File #14668-33 Red #11726

SUPREME COURT OF THE STATE OF NEW YORK

COUNTY OF KINGS

IN THE MATTER

of

65 THE PEOPLE, etc. ex rel. George S. Van Schaick, Superintendent of Insurance, etc. BOND AND MORTGAGE GUARANTEE COMPANY.

IN THE MATTER

of a

Plan of Readjustment, etc. of the rights of the holders of investments in the mortgage guaranteed by Bond and Mortgage Guarantee Company under Guarantee No. 181,568.

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66 IN THE MATTER

of the

Application of the Mortgage Commission of the State of New York, for an order approving a plan for the further readjustment of the rights of holders of investments in a certain mortgage covering premises known as 351 to 363 Marine Avenue, Brooklyn, County of Kings, New York, guaranteed by Bond and Mortgage Guarantee Company under Guarantee No. 181,568, to the extent of appointing a trustee, etc.

Exhibit A, Annexed to Petition 67

The Mortgage Corporation of New York, a corporation organized under the Insurance Law of the State of New York, having its principal office at 42 Broadway, New York City, New York, having been duly appointed Trustee of the property, the subject of the above entitled proceeding, for the benefit of the holders of mortgage participation certificates guaranteed by the above named guarantee company under the above mentioned guarantee designation, by this Declaration of Trust which, by final order in the said proceeding, it is authorized to execute, hereby accepts the appointment as such Trustee, and hereby also declares and agrees as follows: 68

Certificate Holders

I. The term "Certificate Holder" means a holder of a certificate (commonly herein called a Mortgage Certificate) issued in his name and so registered on the books of the issuing company, which evidences the participating interest of the holder with respect to the bond and mortgage (or the bonds and mortgages) guaranteed by the above named guarantee company under the above mentioned guarantee designation, and shall also include a holder of a Trustee's Certificate issued in his name and so registered on the books of the Trustee, against a mortgage certificate surrendered by him or by a predecessor in interest to the Trustee. 69

Trust Estate

The term "Trust Estate" shall include the bond and mortgage (or the bonds and mortgages) against which were issued the Mortgage Certificates guaranteed by the above named guarantee company under the above mentioned guarantee designation, and all property, real, personal or mixed, in any manner and at any time or from time to time acquired on behalf of the Certificate Holders in lieu of or in addition

to the bond and mortgage (or the bonds and mortgages) aforesaid, together with all claims and choses in action which the Certificate Holders as a class have or may have against any person, firm or corporation with respect to any of the property now or formerly included in the Trust Estate.

Receipt of Trust Estate

The Trustee will take, hold, manage and control the property constituting the Trust Estate insofar as the same shall have been transferred to the Trustee or may have become
71 vested in it. The Trustee shall not be required to go into the transactions behind the items of any account or accounting furnished to it either by the guarantee company above named, or the Superintendent of Insurance of the State of New York or the Superintendent of Banks of the State of New York either Superintendent acting as rehabilitator or liquidator, or Mortgage Commission of the State of New York or any subsidiary corporation, agent or successor of any of such parties, where such items appear on their face to be regular and proper; but nothing herein contained shall be construed as in any wise restricting or affecting the right of the Trustee to demand or obtain such further and other accounting as the Trustee in its discretion deems to be
72 to the best interests of the certificate holders. The Trustee shall not be deemed to be relieved of the duty of reducing to possession any property which by the exercise of ordinary diligence it could have ascertained belonged to the Trust Estate.

Powers of Trustee

II. The Trustee is vested with all the rights and powers of an absolute owner of the property from time to time constituting the Trust Estate and may exercise any and all such rights and powers, including, without limiting the gen-

erality of the foregoing, the absolute, full and complete power to receive payments of interest, installments of principal and all other payments which are or may become due to the certificate holders; to enforce the claims of the certificate holders as a class against the above named guarantee company and against any other person, firm or corporation; to accelerate the due date of any bond and mortgage now or at any time an asset of the Trust Estate in accordance with the terms thereof or of any extension or modification agreement made with respect thereto; to obtain an assignment of rents and to manage, control and operate the property covered by any mortgage now or at any time an asset 74
of the Trust Estate; to foreclose any mortgage now or at any time an asset of the Trust Estate; to acquire, either by voluntary conveyance, or through a foreclosure sale, title to the real and/or other property covered by any mortgage now or at any time an asset of the Trust Estate, and, as to any real property, and its appurtenances, equipment and/or furnishings, with respect to which the Trustee may at any time be possessed of title for the benefit of the certificate holders, the Trustee shall have all the rights and powers of an absolute owner thereof and may exercise any and all such rights and powers including, without limitation of the foregoing, the absolute full and complete power to manage, control, 75
operate, repair, improve, rehabilitate and protect such property and pay the expenses thereof out of the income therefrom or out of the funds of the Trust Estate or out of advances made by the Trustee or out of monies borrowed in accordance with the provisions hereof or of the aforementioned final order; to make leases and agreements, reduce rents or otherwise modify present or future leases and agreements; to enforce and compromise claims and receive all debts, rent, income and assets growing out of such property which are or may become due, payable or deliverable from time to time; to discharge any and all liens and charges

against such property out of the income or proceeds thereof; to sell, with the approval of the Court, obtained as hereinafter provided in paragraph III, such property and take back, hold, enforce and protect a purchase money bond and mortgage. The Trustee may make, if it is authorized to engage in such business, or may procure, such title searches and title insurance as it deems advisable and pay the customary and reasonable charges therefor out of the Trust Estate. The Trustee may purchase with the funds in the Trust Estate, such fixtures, furniture and other personal
77 property as, in its opinion, are necessary or advisable for the operation of any real property now or at any time an asset of the Trust Estate. The Trustee shall be under no obligation to enforce any bond and mortgage now or at any time an asset of the Trust Estate, either by foreclosure or otherwise, unless it deems it advisable to do so and there are funds in its possession sufficient, in its opinion, to pay the necessary expenses of such foreclosure or other action or proceeding, or unless one or more certificate holders shall advance to the Trustee sufficient funds for such purpose. If, in the latter event, the Trustee shall deem it inadvisable to foreclose, it shall apply to the Supreme Court for instructions upon at least ten days' notice by mail to all of the
78 certificate holders. Any monies so advanced by any certificate holder or holders shall be repaid, with interest, to the person or persons making such advances, prior to any payment to the certificate holders generally.

Extension—Release—Sale

III. The Trustee shall not extend any bond and mortgage, reduce the rate of interest, release any property from any mortgage except as authorized by the terms thereof or the order above referred to, nor sell the securities or the property covered thereby, without the permission of the Court by order obtained in said reorganization proceeding

after ten days' notice by mail addressed to the certificate holders.

Application for Instructions

IV. The Trustee may apply to the Supreme Court, either *ex parte* or upon such notice as the Court may direct, for any other or further instructions regarding the Trust Estate or the duties of the Trustee hereunder any every such order shall be binding upon all of the certificate holders.

Loans—Advances 80

V. The Trustee may at its option (but shall not be required to) make advances or borrow monies for the purpose of paying taxes, water rates, assessments and/or insurance premiums, employing watchmen or caretakers, making repairs, alterations or improvements, paying expenses of foreclosures and/or the expenses of reorganization, or to purchase fixtures, furniture and other personal property which it deems necessary or advisable for the operation of property of the Trust Estate, which advances or loans, together with interest and the fees of the Trustee, shall be a first lien in favor of the Trustee upon the Trust Estate and may be paid with interest before payments are made to the certificate 81 holders.

Account—Filing—Objections

VI. The Trustee shall annually file an account in the Office of the Clerk of the County in which the above proceeding was instituted, and within ten (10) days after such filing, mail a copy thereof to each certificate holder and to Mortgage Commission of the State of New York, together with a notice setting forth that the said account will be brought on for hearing on a date specified in such notice,

82 *Exhibit A, Annexed to Petition*

which shall be not less than twenty (20) days after the date of the mailing of said account and notice, and that at such time the Court will either approve, modify or reject the said account. Written objection to said account may be filed in the Office of the Clerk of the County in which the Trustee was appointed not less than five (5) days before such return day, and a copy of such objections shall at the same time be served upon the Trustee and the Mortgage Commission. If a certificate holder or other person in interest be not represented by an attorney, the Court may dispense with the filing of objections. The expense of printing
83 and mailing copies of such account shall be deemed an expense of administration and shall be paid by the Trustee out of the Trust Estate. Each such account shall contain a statement of (a) all of the Trustee's income, expenditures and distributions affecting the Trust Estate during the particular year involved, (b) the balance remaining in its hands at the end of such year and (c) its administration of the property. The Trustee in addition thereto, shall file an account in the Supreme Court whenever the holders of two-thirds in amount of such certificates shall file written request for such additional accounting and within thirty (30) days after such written request (but not oftener than once every
84 six months).

Distribution of Income

VII. The Trustee shall pay to the certificate holders at least semi-annually the net income received by it from the Trust Estate (after paying its fees and all expenses and advances and after setting up necessary reserves to operate the trust property).

Notice to Certificate Holders

VIII. All remittances, communications and notices to the certificate holders shall be mailed to each certificate

holder to his address as it appears upon the records of said Trustee, unless any certificate holder shall have filed with the Trustee at its address aforementioned, a written request designating another address for such purpose, whereupon it shall be mailed to the address so designated.

Commissions—Fees

IX. The Trustee by accepting this appointment waives any and all claims to statutory commissions and compensation for its services hereunder and in lieu thereof shall receive and accept, commencing with the next interest 86
period after the closing hereunder, annual compensation equal to one-twelfth of the income distributed to certificate holders but not less than one-quarter of one per cent. (¼ of 1%) per annum and not more than one-third of one per cent. (⅓ of 1%) per annum of the then unpaid principal amount of the bond and mortgage against which said participation certificates were issued; its compensation until the first interest day after the closing hereunder to be at the rate which The Mortgage Corporation of New York has been receiving as servicing agent. In the event that the trust is terminated, the Trustee shall receive compensation at the applicable rate accrued to the date of termination. In the event that there is a junior participating interest in said 87
bond and mortgage not held by the Trustee, then such annual compensation shall be computed on the basis of the senior participation interest in said bond and mortgage. If more than one bond and mortgage is involved in the above entitled proceeding, then, and in that event, the expression "bond and mortgage," wherever above used in this paragraph, shall be regarded as referring to "bonds and mortgages," and the minimum annual compensation of the Trustee shall be not less than one-half of one per cent. (½ of 1%) per annum of the then unpaid aggregate principal amount of such bonds

88 *Exhibit A, Annexed to Petition*

and mortgages. In addition to such annual compensation, the Trustee shall be entitled to a management charge or fee, computed on the basis of the applicable rates set forth in the schedule marked Schedule "A" hereto annexed, and made a part hereof, with respect to any real property at any time held in the Trust Estate or operated by the Trustee for the benefit of the certificate holders pursuant to assignment of rents or otherwise, which management charge or fee it may pay in whole or in part to a managing agent, or retain, as it sees fit; and the Trustee shall not be entitled to any other credit or deduction for payments to any managing agent, ex-
89 cept payments to such an agent of rental commissions in accordance with Schedule "A" hereto annexed. Out of its compensation, above provided for, the Trustee shall pay the fees of any counsel which it may employ to advise it with respect to the administration of the Trust Estate or its duties hereunder or the preparation of any accounting which it may make. The fees and expenses of any counsel which the Trustee may employ in legal proceedings brought in or concerning the enforcement or administration of the trust, or in any action or proceeding to which it is a party, as fixed and determined by the Court upon an application made for such purpose, shall be proper charges against the Trust
90 Estate, and payable out of the assets thereof.

Brokerage Commissions

X. The Trustee may pay to brokers, as operating costs of the Trust Estate, the usual commissions for effecting sales, leases or renewal of leases.

Termination—Modification—Final Account

XI. This trust shall continue until the Trust Estate has been fully liquidated, except that at any time prior thereto, this trust, with the approval of the Supreme Court, upon the

consent thereto, in writing duly acknowledged, of the holders of two-thirds of the principal amount of the certificates, may be modified (with the consent of the Trustee) or terminated or the Trustee removed and a successor Trustee appointed. Within sixty days after the full liquidation of the Trust Estate, or in liquidation so far as the Trustee finds itself able to accomplish that end, the Trustee shall render and file with the Court its final account and mail copies thereof to all of the certificate holders at their last known addresses together with a notice of motion setting forth the time when and the place where an application to the Court for confirmation and approval of such account, the termination of the trust and the discharge of the Trustee will be made. Any assets of the Trust Estate left remaining in the hands of the Trustee shall be disposed of as the Court may direct in the order entered on such application. 92

Resignation of Trustee

The Trustee may resign at any time by obtaining leave of the Court after giving the certificate holders at least thirty days' notice by mail of its intention to apply for such resignation, and if such resignation is approved by the Court, the Court will appoint its successor. In the event of the resignation or removal of the Trustee, it shall within sixty days thereafter file its final account with the Court and mail copies thereof to all registered holders of certificates, and said Trustee shall dispose of any funds or property held by it as the Court shall direct. 93

Trust Funds Only Liable

XII. Any one contracting with the Trustee shall look only to the funds and property of the Trust Estate for payment under such contract.

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94 *Exhibit A, Annexed to Petition*

Registration of Certificates

XIII. Each holder of a mortgage certificate shall present his mortgage certificate to the Trustee for registration by it and for a notation thereon that the rights of the holder thereof are subject to all of the provisions of this Declaration of Trust, to the Plan of Reorganization, as approved, respecting the mortgage investment here concerned and to the proceedings of the Supreme Court pursuant to which this Declaration of Trust has been executed. All funds and other benefits payable in respect to mortgage certificates not
95. so registered, shall be set aside by the Trustee in a special fund to be paid over, but without interest, to the owner of the mortgage certificate in respect of which such funds are applicable, upon the due registration of such certificate with the Trustee.

Transfer of Certificates

XIV. Any party who has rightfully acquired, by purchase or otherwise, a mortgage certificate issued in the name of another, may surrender such certificate to the Trustee duly endorsed or assigned for transfer, and receive therefor a Trustee's Certificate with respect thereto, issued in his name and so registered on the books of the Trustee. Such Trustee's
96 Certificate shall contain a statement to the effect that the said mortgage certificate has been surrendered to the Trustee, that the Trustee holds the same for the account of the registered holder and owner of the Trustee's Certificate issued and outstanding against said mortgage certificate and that the party in whose name the Trustee's Certificate is issued, is registered on the books of the Trustee as the registered holder of said Trustee's Certificate and that the rights of such party in and to such mortgage certificate are subject to all of the provisions of this Declaration of Trust, to the

Plan of Reorganization, as approved, respecting the mortgage investment here concerned, and to the proceedings of the Supreme Court pursuant to which this Declaration of Trust has been executed. The Trustee's Certificate shall also contain such other or further statements or recitals as the Trustee deems proper and it shall be transferable only on the books of the Trustee, upon surrender of the certificate transferred.

Lost, etc. Certificates—Indemnity Bond

Any holder who has lost his mortgage certificate or whose 98
mortgage certificate has been destroyed, mutilated or stolen, may become a registered holder, in case his certificate has not been registered with the Trustee prior to such destruction, loss, mutilation or theft, and any certificate holder shall be entitled to receive from the Trustee a Trustee's Certificate in such form as the Trustee may prescribe, evidencing his rights in and to such mortgage certificate, by furnishing to the Trustee (1) his sworn affidavit with respect to such loss, destruction, mutilation or theft, in such form and detail as may be prescribed by the Trustee, and (2) an indemnity bond in such amount as may be required by the Trustee, and issued by a surety company or other indemnitor
or indemnitors acceptable to the Trustee. In a situation 99
involving a mutilated certificate, the Trustee may require the surrender of such mutilated certificate as a condition to the issuance of its Certificate.

Any party who subsequently rightfully acquires, by purchase or otherwise, any Trustee's Certificate issued as aforesaid, may in turn surrender same to the Trustee duly endorsed or assigned for transfer, and received therefor a Trustee's Certificate in similar form, issued in his name and so registered on the books of the Trustee.

100 *Exhibit A, Annexed to Petition*

Trustee May Make Regulations for Registration, etc.

The Trustee may make such rules respecting the registration of mortgage certificates and the issuance and transfer upon its books of the Trustee's Certificates above provided for as it may deem reasonable and proper, and among other things it may require, (1) the payment of any transfer taxes and other governmental charges required to be paid in the matter, (2) the registration of the mortgage certificate involved in conformity with paragraph XIII hereof and (3) compliance with the practice, custom and procedure prevail-
101 ing in the City of New York in connection with the transfer of stocks and bonds. The Trustee may close its books for the registration of Trustee's Certificates or for the transfer of such certificates, for five days immediately prior to any periodic distribution of principal or income of the Trust Estate to certificate holders. The Trustee may permit two or more persons to be a registered holder under this trust of the same mortgage certificate and of a Trustee's Certificate and the recital of the rights of a holder here given in the singular shall include the rights in proportion to their interest when two or more persons are the registered holders on the books of the Trustee or the holder of a Trustee's Certificate or of an undivided interest in a mortgage certifi-
102 cate and in a Trustee's Certificate issued in respect thereto.

Participation of Guarantee Company

XV. Until a final judgment of a Court of competent jurisdiction shall have been obtained determining to what extent, if any, the participation of the above mentioned guarantee company in the guaranteed mortgage investment shall be entitled to the benefits of this trust, the pro rata share of said guarantee company in the Trust Estate in the net income and/or the net proceeds of the sale or liquidation

thereof shall be retained by the Trustee and deposited in a separate account, the same not to bear interest.

Deposit of and Interest on Trust Funds

XVI. The Trustee may keep moneys belonging to the Trust Estate on deposit in any bank or trust company in New York City, and shall not be under any obligation to pay interest on such moneys on deposit in such bank or trust company. The Trustee may commingle moneys belonging to the Trust Estate with moneys belonging to any other trust estate held under a Declaration of Trust substantially similar to this one, but shall not mingle moneys belonging to the Trust Estate with its own general funds. 104

Holding of Trust Property

XVII. The Trustee may hold in its own name as Trustee any or all of the property of the Trust Estate or in the exercise of its discretion and, with the approval of the Court, obtained either *ex parte* or upon such notice as the Court may direct, may hold any of such property in the name of an individual, partnership or corporation as its nominee, but it shall be responsible for the acts of such nominee. The cost of forming a corporation to act as such nominee, and the annual franchise taxes or other taxes of such corporation shall be proper expenses of the Trust Estate, if allowed by the Court. 105

Acceptance of H.O.L.C. bonds, etc.

XVIII. The Trustee may satisfy or assign any bond and mortgage at any time held in the Trust Estate in consideration of Home Owners' Loan Corporation bonds, or bonds issued by any other Federal or State agency provided the same are in an amount equal to the then unpaid principal

amount owing on said bond and mortgage with accrued interest. The Trustee may, with the approval of the Court, with or without notice to certificate holders as the Court may direct, satisfy or assign any bond and mortgage any time held in the Trust Estate in consideration of Home Owners' Loan Corporation bonds, or bonds issued by any other Federal or State agency, in an amount less than the then unpaid principal amount of said bond and mortgage and accrued interest.

Who Bound

107 XIX. This Declaration of Trust is binding upon the Trustee herein named and its successor, and upon all certificate holders whether such certificates are registered with the Trustee as herein provided or not, their respective heirs, executors, administrators, successors and assigns.

IN WITNESS WHEREOF, THE MORTGAGE CORPORATION OF NEW YORK as the Trustee herein named has caused this Indenture to be executed by its duly authorized officer and its corporate seal to be affixed this 12th day of December, 1938.

108 By (SIGNED) P. E. BENNETT
President

[SEAL]

By (SIGNED) C. H. HEINLEIN
Secretary

Exhibit A, Annexed to Petition 109

STATE OF NEW YORK, }
COUNTY OF NEW YORK, } ss.:

On this 12th day of December, 1938, before me personally came P. E. BENNETT, to me known, who being by me duly sworn, did depose and say that he resides at 66—78th Street, Brooklyn, New York; that he is President of THE MORTGAGE CORPORATION OF NEW YORK, the corporation described in and which executed the foregoing instrument; that he knows the seal of said corporation and that the seal affixed to said instrument is such corporate seal; that it was so affixed by order of the Board of Directors of said corporation and that 110
he signed his name thereto by like order.

H. F. WILLIAMS JR.
Notary Public, Queens County
Queens Co. Reg. No. 4876, Clerk's No. 2096
Kings Co. Reg. No. 9008, Clerk's No. 3
New York Co. Reg. No. 9W20 Clerk's No. 19
Nassau Co. Clerk's No. 9W6
Certificate Filed in Suffolk County
Term Expires March 30, 1939

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112 EXHIBIT D, ANNEXED TO PETITION

At a Special Term Part VII (formerly the Additional Special Term) of the Supreme Court of the State of New York, held in and for the County of Kings, at the County Court House, in the Borough of Brooklyn, City of New York, on the 5th day of December, 1938.

Present:

HON. GEORGE E. BRUWER,
Justice.

113 IN THE MATTER
of the
Application of the People of the State of New York, by George S. Van Schaick, Superintendent of Insurance of the State of New York, for an order to take possession of the property of and rehabilitate the Bond and Mortgage Guarantee Company.

IN THE MATTER
of a
Plan of readjustment etc. of the rights of the holders of investments in a certain mortgage covering premises 351 to 363 Marine Avenue, Brooklyn, New York, guaranteed by Bond and Mortgage Guarantee Company, Guarantee No. 181,568.

114 IN THE MATTER
of the
Application of the Mortgage Commission of the State of New York, for an order approving a plan for the further readjustment of the rights of holders of investments in a certain mortgage covering premises 351 to 363 Marine Avenue, Brooklyn, New York, guaranteed by Bond and Mortgage Guarantee Company, Guarantee No. 181,568, to the extent of appointing a trustee of the bond, mortgage or other security against which such mortgage investments were issued, and defining the powers and duties of such Trustee, and modifying the final order approving the original plan of readjustment of the rights of the holders of investments in said mortgage.

FINAL ORDER No. 270 M

Exhibit D, Annexed to Petition 115

The Legislature of the State of New York by Chapter 745 of the Laws of 1933, as amended, and Chapter 19 of the Laws of 1935, as amended, having duly declared the existence of a public emergency affecting the health, safety and comfort of the People of the State of New York, and Mortgage Commission of the State of New York, having duly formulated and promulgated a plan (referred to in these proceedings as the "Modified Plan") to effect the further readjustment, modification or reorganization of the rights of the holders of investments represented by guaranteed mortgage participation certificates in a certain mortgage covering premises 351 to 363 Marine Avenue, Brooklyn, City and State of New York, to 116
the extent of appointing a Trustee of the bonds, mortgages and other security against which such mortgage investments have been issued, and transferring to such Trustee the title to such bonds, mortgages and other security upon such trusts, terms and conditions as are set forth in the Modified Plan of readjustment, etc., and due notice of a hearing upon such Modified Plan having been duly given by Mortgage Commission of the State of New York to the holders of all mortgage investments represented by participation certificates in said mortgage and to all persons, firms, associations or corporations known to Mortgage Commission to have an interest which might be affected by the proposed Modified Plan, and 117
the hearing upon such notice having come on regularly to be heard before this Court on the 27th day of June, 1938, at 10 A. M., at the County Court House, in the Borough of Brooklyn, City and State of New York, and Mortgage Commission of the State of New York, having duly appeared by Maurice Finkelstein (James F. Donlan and Benjamin Harwood Jr., of counsel) Louis H. Pink, Superintendent of Insurance of the State of New York, as Liquidator of Bond and Mortgage Guarantee Company, having duly appeared by J. Donald Whelehan, Title Guarantee and Trust Company having duly appeared by C. Elmer Spedick (Edward F. Kiernan, of counsel) The Mortgage Corporation of New York having

118 *Exhibit D, Annexed to Petition*

duly appeared by Hughes, Richards, Hubbard & Ewing (Curtiss E. Frank, of counsel) a Committee of Holders of Guarantees of Bond and Mortgage Guarantee Company having duly appeared by Herrick & Feinstein (Abraham Feinstein, of counsel)

Now, upon reading and filing the notice given by Mortgage Commission of the State of New York, dated June 1, 1938, the Modified Plan annexed thereto promulgated by Mortgage Commission of the State of New York, the affidavit of George I. Bauman, Special Supervisor of Mortgage Com-
119 mission of the State of New York, sworn to June 22, 1938, the annexes A, B and B-1 attached thereto, the written consents of the holders of two-thirds in principal amount of such mortgage investments (exclusive of any part thereof held by the guaranty corporation which sold or guaranteed such mortgage investments), the testimony of the witnesses appearing at said hearing, the exhibits received in evidence, and the approval of the Modified Plan by the Mortgage Commission of the State of New York having been given in open court, and, upon all plans, orders and proceedings heretofore had herein,

And it appearing to my satisfaction that heretofore, pur-
120 suant to Sections 3 and 4 of Chapter 745 of the Laws of 1933 of the State of New York, as amended, the Superintendent of Insurance exercised the powers therein granted him and took over all the functions of Bond and Mortgage Guarantee Company with respect to each mortgage investment sold or guaranteed by that Company, including the mortgage investments involved in this proceeding, and that heretofore the Superintendent of Insurance of the State of New York, pursuant to the powers vested in him under said Chapter 745 of the Laws of 1933 as amended, duly instituted and brought on for hearing before the Supreme Court of the State of New York, County of Kings, a special proceeding to secure judicial action upon a plan of readjustment, modification or reorganization of the rights of the holders of investments in the above

described mortgage (referred to in these proceedings as the "Original Plan"), which Original Plan after due hearing was approved by this Court and declared binding upon all holders of investments and other interested parties therein by a final order entered in the office of the Clerk of the County of Kings, which Original Plan and order did not provide for the appointment of a trustee of the bond and mortgage and other security against which such mortgage investments were issued and did not transfer the title of such bond, mortgage and other security to a trustee; that no trustee of the bond and mortgage against which these mortgage 122
investments were issued has ever been appointed; that the mortgage investments did not at any time come into the control of the Mortgage Commission of the State of New York pursuant to Section 6 of Article IV of the Mortgage Commission Act; that Mortgage Commission of the State of New York promulgated the aforementioned Modified Plan of readjustment under date of June 1, 1938, pursuant to Chapter 745 of the Laws of 1933 of the State of New York, as amended; that Mortgage Commission obtained a list of the holders of the mortgage investments in said mortgage from The Mortgage Corporation of New York, which corporation as successor servicing agent to Bond and Mortgage Guarantee Company now maintains the list of such holders previ- 123
ously kept by Bond and Mortgage Guarantee Company; that Mortgage Commission submitted such Modified Plan to all the holders of mortgage investments named on said list and to all other persons, firms, associations or corporations known to Mortgage Commission to have an interest which might be affected by said Modified Plan by mailing a copy of the said Modified Plan, postage prepaid, to each such holder addressed to him at the address set forth in said list and to the said other persons, firms, associations or corporations at the last address of such persons, firms, associations or corporations as known to Mortgage Commission, together with a notice stating in substance that the said Modified Plan would be presented to this Court on a date which was not

124 *Exhibit D, Annexed to Petition*

less than twenty (20) days after the mailing of such plan and notice, and that upon such date this Court would pass upon such Modified Plan and hear any objection thereto on the part of any holder of any such mortgage investment or such other party as might have an interest therein; that, since the date of the mailing of said Modified Plan and notice, a copy thereof has been kept by Mortgage Commission of the State of New York at its office, 346 Broadway, New York, N. Y., available for public inspection, and that more than two-thirds of the holders in principal amount of such mortgage investments (exclusive of any part thereof held by the
125 guaranty corporation which sold or guaranteed such mortgage investments) have given their written consent to such Modified Plan, and that such Modified Plan was approved by this Court by interlocutory order granted on the 23rd day of July, 1938;

Now, on application of Maurice Finkelstein, Esq., attorney for Mortgage Commission of the State of New York, it is

Ordered that the said Modified Plan providing for the further readjustment, modification and reorganization of the rights of the holders of mortgage investments represented by guaranteed mortgage participation certificates in the mort-
126 gage covering premises known as 351 to 363 Marine Avenue, Brooklyn, New York, as promulgated by Mortgage Commission of the State of New York, and approved by this Court, is hereby declared to be binding upon all the holders of mortgage investments in said mortgage, the Superintendent of Insurance of the State of New York, as Liquidator of Bond and Mortgage Guarantee Company, Title Guarantee and Trust Company, The Mortgage Corporation of New York, the owner or owners of the underlying real estate, and all other parties interested therein, and it is further

Ordered that The Mortgage Corporation of New York be and it hereby is appointed Trustee of all the property constituting the Trust Estate; and it is further

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ORDERED that Title Guarantee and Trust Company be and it hereby is authorized and directed forthwith to assign, transfer, set over and deliver unto The Mortgage Corporation of New York, as Trustee, in so far as the same shall be in its possession or control, the said bonds and mortgages and any and all assignments thereof (with adequate instruments for the transfer thereof to the said Trustee "without recourse" and in form sufficient for recording) and shall also assign, transfer and deliver unto the said Trustee all cash and other property, real, personal or mixed, securing or intended to secure the certificates issued against the mortgage which is the subject matter of this proceeding, together with a certified list of the holders of such certificates; and Mortgage Commission of the State of New York be and it hereby is authorized and directed to execute any and all such instruments as may be necessary or desirable to effectuate such transfer; and it is further

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ORDERED that upon the execution of the assignment provided for in this order, the agency of The Mortgage Corporation of New York to service the mortgage investments herein as provided for in the Original Plan and the order or orders approving same shall terminate, and Title Guarantee and Trust Company, Mortgage Commission of the State of New York and The Mortgage Corporation of New York be and they hereby are authorized and directed to take such steps as may be necessary to cancel any servicing agreement entered into by these parties pursuant to the order of this Court approving the Original Plan; and it is further

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ORDERED that the said Trustee be and it hereby is authorized and directed to execute, as soon as reasonably convenient after the entry of this order, a declaration of trust, substantially in the form annexed to the notice of proceeding herein and marked Exhibit "A", with such modifications of a non-substantial nature as the attorneys for the Trustee

and the attorneys for the Mortgage Commission of the State of New York may deem necessary; and it is further

ORDERED that any provisions of the Original Plan or of the order or orders approving same, which are inconsistent with the provisions of this Modified Plan as approved by this Final Order be and the same hereby are in all respects superseded by the provisions of this Modified Plan as approved and declared binding by this Final Order, and that the Original Plan and the order or orders approving same be and they hereby are modified by this Modified Plan as
131 approved and declared binding by this Court; and it is further

ORDERED that all interested parties be and they hereby are authorized and directed to execute any and all papers, instruments and/or documents, and do all things necessary or desirable to effectuate the consummation of said Modified Plan hereby approved and declared to be binding; and it is further

ORDERED that this Court, having assumed jurisdiction of this proceeding, shall retain jurisdiction hereof until the complete liquidation of the Trust Estate and the termination of the trust; and the Trustee, or any other interested party
132 herein, may apply at the foot of this Final Order upon such notice as the Court may direct for such other and further relief as to the Court may seem just and proper.

Enter

GEO. E. BROWER
J. S. C.

Granted
December 6, 1938

JOHN N. HARMAN
Clerk

EXHIBIT E, ANNEXED TO PETITION. 133

SUPREME COURT OF THE STATE OF NEW YORK

COUNTY OF KINGS.

IN THE MATTER

of the

Application of the PEOPLE OF THE STATE OF NEW YORK, by George S. Van Schaick, as Superintendent of Insurance of the State of New York, for an order to take possession of the property of and rehabilitate the

BOND AND MORTGAGE GUARANTEE COMPANY.

IN THE MATTER

of a

Plan of readjustment, etc., of the rights of the holders of investments in a certain mortgage covering premises *351 to 363 Marine Avenue,* Brooklyn, New York, guaranteed by Bond and Mortgage Guarantee Company, Guarantee No. *181,568.*

134

NOTICE OF PROCEEDING UNDER CH. 745 OF THE LAWS OF 1933, AS AMENDED

No. 270

135

Sir:

A plan for the readjustment, modification or reorganization of the rights of the holders of investments in a mortgage covering premises *351 to 363 Marine Avenue,* Brooklyn, New York, guaranteed by Bond and Mortgage Guarantee Company (Guarantee No. *181,568*) has been promulgated by George S. Van Schaick, Superintendent of Insurance of the

136 *Exhibit E, Annexed to Petition*

State of New York, he having heretofore exercised the powers granted to him under Sections 3 and 4 of Chapter 745 of the Laws of 1933, as amended.

A copy thereof is herewith submitted to you by the Superintendent of Insurance of the State of New York, pursuant to the provisions of Section 6 of Chapter 745 of the Laws of 1933, as amended.

A copy of said plan will be kept by me, the Superintendent of Insurance, at my office at 160 Broadway, New York, N. Y., and a copy of said plan and the agreement relating
137 thereto will be kept at Bond and Mortgage Guarantee Company, Certificate Reorganization Division, 16 Court Street, Brooklyn, N. Y.

PLEASE TAKE NOTICE that such plan will be presented to the Supreme Court, Kings County, at an *Additional Special Term* thereof, to be held on *October 24, 1934, at 10* o'clock in the forenoon of that day or as soon thereafter as counsel can be heard before Mr. Justice George E. Brower, one of the Justices of said Court, in the Special Term, Part VI Courtroom, in the County Court House, at Joralemon and Fulton Streets, in the Borough of Brooklyn, City and State of New York, at which time the Court will pass upon such
138 plan and hear any objection thereto on the part of any holder of such mortgage investment, or on the part of any other party as may have an interest thereunder; and hear and pass upon such other and further proposals for the benefit of certificate holders as the Court may deem proper; and

PLEASE TAKE FURTHER NOTICE that at such time the Court will be asked to enter an order approving, modifying or disapproving such plan or agreement and in the event of an order approving such plan as submitted or modified to enter an order providing that such plan so approved shall be binding upon all holders of investments in said mortgage upon satisfactory proof of the fact that 66⅔ per centum of the

holders in principal amount of such holders shall have approved the same.

Dated: September 21, 1934.

Yours, etc.,

GEORGE S. VAN SCHAICK,
Superintendent of Insurance of the State of New York.

HUGHES, SCHURMAN & DWIGHT,
Attorneys for said Superintendent of Insurance, 140
100 Broadway,
Borough of Manhattan,
City of New York.

To:

ALL HOLDERS OF INVESTMENTS IN SAID MORTGAGE.

BOND AND MORTGAGE GUARANTEE COMPANY,
16 Court Street,
Brooklyn, N. Y.

TITLE GUARANTEE AND TRUST COMPANY,
176 Broadway,
New York City.

C. ELMER SPEDICK, Esq., 141
26 Court Street,
Brooklyn, N. Y.

JAMES D. MCCAULEY, Esq.,
100 Broadway,
New York, N. Y.

BOND AND MORTGAGE GUARANTEE CORPORATION,
c/o Mr. B. J. O'Brien,
16 Court Street,
Brooklyn, N. Y.

MARINE HARBOR PROPERTIES, INC.,
1441 Broadway,
New York, N. Y.

142 *Exhibit E, Annexed to Petition*

Plan for the Readjustment, Modification or Reorganization of the Rights of All the Holders of Investments in a Certain Mortgage, Covering Premises *351 to 363 Marine Avenue,* Borough of Brooklyn, City and State of New York, and Guaranteed by Bond and Mortgage Guarantee Company, Designated as Guarantee No. *181,568* of That Company.

I, GEORGE S. VAN SCHAICK, Superintendent of Insurance of the State of New York, having heretofore exercised the powers granted to me under Sections 3 and 4 of Chapter
143 745 of the Laws of 1933 of the State of New York as amended, hereby promulgate the following plan for the readjustment, modification and reorganization of the rights of the holders in the mortgage investments above described pursuant to Chapter 745 of the Laws of 1933 of the State of New York as amended.

PRESENT STATUS OF THE MORTGAGE

The property affected by the mortgage is located at 351 to 363 Marine Avenue, in the Borough of Brooklyn, County of Kings, City and State of New York, and consists of an irregular plot of land on the northwest corner of Marine Ave-
144 nue and 4th Avenue, having a frontage on Marine Avenue of 214 feet, and approximately 214 feet in the rear thereof, and a frontage on 4th Avenue of approximately 114 feet, and 122 feet in the rear thereof. There is erected on said plot a six-story and cellar brick, store and apartment building, containing three stores and 312 rooms, subdivided into 103 apartments.

The mortgage is in the present sum of $370,000.00, bears interest at the rate of six per centum (6%) per annum and will mature on December 1, 1934.

The mortgage is held by Title Guarantee and Trust Company, of record, against which there were issued by said Trust

Company mortgage participation certificates to ninety-seven (97) holders.

The present owner of the property is Marine Harbor Properties, Inc., whose address is 1441 Broadway, New York, N. Y. The owner states that the Marine Building Corporation, the present obligor on the bond, is financially irresponsible and will not execute the extension agreement hereinafter mentioned.

The arrears against these premises at September 21, 1934, consisted of the balance of the April 1, 1934 tax, in the sum of $3,372.75. The second half of the 1934 tax, in the amount of $5,409.25, will become due and payable October 1, 1934. On the same day, semi-annual interest in the sum of $11,100 will be due.

PLAN OF REORGANIZATION

Term:

The time for the payment of the unpaid principal amount of the mortgage shall be extended for an additional period of two years and four months from December 1, 1934, the present maturity date, to April 1, 1937.

Interest:

The interest payable by the owner upon the unpaid principal amount of the mortgage shall be at the rate of five per centum (5%) per annum from April 1, 1934 to April 1, 1937, the extended maturity date.

Arrears and Accruing Charges:

The owner has agreed, pending the approval of this plan, to pay on the first day of each and every month, a sum equivalent to one-twelfth of the annual charges of interest, taxes, water rates and assessments. The owner further agrees, simultaneously with the proper delivery of the extension agree-

148 *Exhibit E, Annexed to Petition*

ment hereinafter mentioned, to pay all arrears of interest, taxes, water rates and assessments that may be unpaid at that time. Thereafter interest is to be payable semi-annually on the first days of April and October of each year, and all taxes, water rates and assessments are to be paid promptly when the same shall become due and payable.

Extension Agreement:

The owner has agreed to execute, acknowledge and de-
149 liver an extension agreement upon the foregoing terms and including other appropriate provisions not inconsistent therewith. Form of the proposed extension agreement will be filed with the Court as part of the record in this proceeding. Upon approval of this plan, the Court will be requested to direct Title Guarantee and Trust Company, upon the execution and delivery of said extension agreement by the owner and upon payment by the owner of the recording fees and revenue stamps thereon, if any, to execute and deliver the same as record holder of such mortgage.

Service:

The agency of the Bond and Mortgage Guarantee Com-
150 pany to service the mortgage will be revoked and Bond and Mortgage Guarantee Corporation will be appointed to service the mortgage during the extended period thereof. A form of the proposed servicing agreement will be filed with the Court as a part of the record in this proceeding. Upon the approval of this plan, the Court will be requested to direct Title Guarantee and Trust Company, as mortgagee of record, to enter into such servicing agreement with Bond and Mortgage Guarantee Corporation. The Court may, upon application of sixty-six and two-thirds per centum (66⅔%) in amount of the holders of investments in said mortgage, substitute a different servicing agent.

Exhibit E, Annexed to Petition 151

Service Charges:

The servicing agent shall be entitled to deduct and retain from the interest payments collected a sum equal to one twelfth (1/12) of such payments, as its servicing fee or charge.

Guarantee:

The guarantee of Bond and Mortgage Guarantee Company as evidenced by its existing guaranty policy covering this mortgage shall be continued for the extended period of the mortgage, but the guarantee shall be limited to the unpaid balance of principal and to the interest rate to be received by the certificate holders under this plan as finally approved. The Bond and Mortgage Guarantee Company has agreed that the employment of the Bond and Mortgage Guarantee Corporation as servicing agent shall not operate as such a revocation of its agency as would entitle it to claim that the policy of guarantee has been terminated. By consenting to this extension, the Superintendent of Insurance of the State of New York as Rehabilitator of Bond and Mortgage Guarantee Company is not adopting or agreeing to adopt the above numbered guarantee as the undertaking or obligation of the Rehabilitator, and the holders thereof acquire no priority or preference to payment out of the assets of Bond and Mortgage Guarantee Company which they did not have prior to this extension. 152 153

Expenses:

The owner has agreed to pay Bond and Mortgage Guarantee Company a reorganization fee and accordingly no charge or assessment will be made against certificate holders for disbursements or other expenses involved in this proceeding.

Dated: New York, September 21, 1934.

GEORGE S. VAN SCHAICK,
Superintendent of Insurance of the
State of New York

154

EXHIBIT G, ANNEXED TO PETITION

At an Additional Special Term of the Supreme Court of the State of New York, held in and for the County of Kings, at the County Court House, in the Borough of Brooklyn, City of New York, on the 28 day of November, 1934.

Present:

Hon. GEORGE E. BROWER,
Justice.

155

IN THE MATTER
of the
Application of the PEOPLE OF THE STATE OF NEW YORK, by George S. Van Schaick, as Superintendent of Insurance of the State of New York, for an order to take possession of the property of and rehabilitate the
BOND AND MORTGAGE GUARANTEE COMPANY.

IN THE MATTER
156
of a
Plan of readjustment, etc., of the rights of the holders of investments in a certain mortgage covering premises 351 to 363 Marine Avenue, Brooklyn, New York, guaranteed by Bond and Mortgage Guarantee Company, under Guarantee No. 181,568.

FINAL ORDER No. 270

A proceeding having been duly instituted by George S. Van Schaick, Superintendent of Insurance of the State of

New York, to obtain judicial approval of a plan of readjustment, modification and reorganization of the rights of the holders of mortgage investments represented by guaranteed mortgage participation certificates in a certain mortgage made by Marine Building Corporation to Title Guarantee and Trust Company, dated April 28, 1931, covering premises 351 to 363 Marine Avenue, Brooklyn, New York, and the said proceeding having come on regularly to be heard before this Court on the 24th day of Octbber, 1934 at 10 A. M., at the County Court House, in the Borough of Brooklyn, City of New York, and an interlocutory order therein having been entered the 24th day of November, 1934, and it now appearing to the satisfaction of this Court that more than two-thirds of the holders of said mortgage investments (exclusive of any part thereof held by the guarantee company which sold or guaranteed such mortgage investments) have given their written consent to the said plan which said consents have been filed with this Court as part of the record in this proceeding, 158

Now, upon motion of Hughes, Schurman & Dwight, Esqs., attorneys for George S. Van Schaick, Superintendent of Insurance of the State of New York, as Rehabilitator of Bond and Mortgage Guarantee Company, it is 159

ORDERED, that the said plan providing for the readjustment, modification and reorganization of the rights of the holders of investments represented by guaranteed mortgage participation certificates in the mortgage covering premises 351 to 363 Marine Avenue, Brooklyn, New York, as promulgated and approved by the Superintendent of Insurance of the State of New York and presented to and approved by this Court by an order dated the 23rd day of November, 1934, is hereby declared to be binding upon all the holders of investments in said mortgage, upon Bond and Mortgage

160 *Exhibit G, Annexed to Petition*

Guarantee Company, upon Title Guarantee and Trust Company, mortgagee of record, and Marine Harbor Properties, Inc., the owner of the mortgaged premises, and upon all other parties interested therein, and Title Guarantee and Trust Company, as mortgagee of record is hereby authorized and directed to execute with Marine Harbor Properties, Inc., the owner, an extension agreement in the form submitted to the Court at the time of the hearing of the plan referred to, received in evidence and marked as one of the Superintendent's exhibits and filed in the office of the Clerk
161 of the County of Kings, with such modifications as may be necessary to conform with any amendments approved by the Court; and it is further

ORDERED, that any and all documents necessary or convenient in the consummation of said plan of readjustment be executed.

Enter,

GEO. E. BROWER
J. S. C.

Granted
162 Dec. 5, 1934

JOHN N. HARMAN
Clerk

Sir:

PLEASE TAKE NOTICE that an order of which the within is a copy, was entered herein in the office of the Clerk of the County of Kings on the 6 day of Dec., 1934.

Dated, Dec. 6, 1934.

Yours, etc.,

HUGHES, SCHURMAN & DWIGHT,
Attorneys for George S. Van Schaick, Superintendent of Insurance of the State of New York as Rehabilitator of Bond and Mortgage Guarantee Company,

Office and Post Office Address:
100 Broadway,
Borough of Manhattan,
New York City.

To:

County Clerk's Index
No. 14668, 1933

SUPREME COURT
COUNTY OF KINGS.

IN THE MATTER
of the
Application of the PEOPLE OF THE STATE OF NEW YORK, by George S. Van Schaick, as Superintendent of Insurance of the State of New York, for an order to take possession of the property of and rehabilitate the
BOND AND MORTGAGE GUARANTEE COMPANY.

COPY
In the Matter of a Plan of Readjustment, etc., of a Mortgage Covering Premises:
351 to 363 Marine Avenue, Brooklyn, New York
Guarantee No. 181,568
Final Order 270

HUGHES, SCHURMAN & DWIGHT,
Attorneys for George S. Van Schaick, Superintendent of Insurance of the State of New York as Rehabilitator of Bond and Mortgage Guarantee Company,
Office and Post Office Address:
100 Broadway,
Borough of Manhattan,
New York City.

Due and timely service of a copy of the within is hereby admitted this .... day of ....., 193...

Notice of Entry to:

C. ELMER SPEDICK, ESQ.
Attorney for Title Guarantee and Trust Company
26 Court Street
Brooklyn, N. Y.

Marine Harbor Properties, Inc.,
1441 Broadway,
New York, N. Y.

Owner.

COPY RECEIVED
DEC 8 1934
C. ELMER SPEDICK

Attorney for.....

166 EXHIBIT K, ANNEXED TO PETITION

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

IN THE MATTER *of* MARINE HARBOR PROPERTIES, INC., *Debtor.*	AFFIDAVIT PLAN No. 270 BMC 181568

167 STATE OF NEW YORK, }
COUNTY OF NEW YORK, } ss.:

JOSEPH L. LONG, being duly sworn, deposes and says:

I reside at 1426 East 15th Street, Borough of Brooklyn, New York. I am now, and for more than five years have been, employed as a real estate appraiser by The Mortgage Corporation of New York. I have been engaged in the business of appraising real estate in New York City and the metropolitan area for more than twenty years and have qualified as an expert with respect thereto in many judicial proceedings. My opinion has also been used on numerous occasions
168 as the basis for making loans upon, and sales of real estate in this locality.

On March 15th, 1940, I personally inspected and appraised premises located at the Northwest corner of Marine and Fourth Avenues, in the Borough of Brooklyn, County of Kings, City and State of New York, also known as 351-363 Marine Avenue. The property consists of a plot of ground 214 feet by 114.5½ feet, irregular, improved by a six story and cellar brick elevator apartment building containing 309 rooms, subdivided into 103 apartments, and three stores; and was erected in 1930. The building is equipped with a steam heating plant, which also supplies hot water. The building

169

contains two Seaberg self-service elevators, two incinerators and has two iron stairways. The lobby and hall floors are of terrazzo and the baths have colored tile walls 4 feet 6 inches high and tile flooring. The rooms have 7/8 inch parquet oak flooring throughout with the exception of the kitchens.

I am of the opinion that as of March 15th, 1940, the property had a fair value of $350,000.00 of which $65,000.00 was applicable to the land and $285,000.00 to the building and improvements thereon. The property was assessed in 1941-42 for $380,000.00 of which $90,000.00 was applicable to the land and the balance thereof to the building and improvements thereon.

170

JOSEPH L. LONG

Sworn to before me this
25 day of Sept. 1941.

Signed) SAMUEL E. ZALOUM
Notary Public, Kings Co.
N. Y. Co. Clerk's No. 27
N. Y. Co. Reg. 3-Z-19
Commission expires March 30, 1943.

171

172

Affidavit of Curtiss Ely Frank

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

[SAME TITLE]

STATE OF NEW YORK,
COUNTY OF NEW YORK, } ss.:

173

CURTISS ELY FRANK, being duly sworn, deposes and says:

I am a member of the firm of Hughes, Hubbard & Ewing, attorneys for The Mortgage Corporation of New York, Trustee of the first mortgage in the above entitled matter. I make this affidavit in support of an application by such Trustee to dismiss the proceeding under Chapter X of the Bankruptcy Act.

I have been in charge of this mortgage trust for some time and have had frequent dealings with the president of the debtor corporation. He has on several occasions during
174 the foreclosure receivership promised that he would make definite arrangements to clear up the arrears and vacate the receivership if certain delays in the receivership proceedings were granted. First, he wished delay on a motion authorizing the receiver to make certain necessary repairs. He failed to keep his promises and the order was eventually entered. Thereafter he requested further delay and a minimizing of expense, stating to me that the money had been raised and that he would be here at three o'clock on a Monday afternoon with the money to close up the entire matter. He failed to appear. Several days later he called and apologized and said that he would be in at a subsequent date.

Again, he failed to appear. Thereafter I investigated and was informed by my associates and by employees of The Mortgage Corporation of New York that he had been thoroughly unreliable throughout.

CURTISS ELY FRANK.

Sworn to before me this
29th day of September, 1941.

MARGARET ELEANOR WALLING
Notary Public 176
N. Y. Co. Clk's No. 30, Reg. No. 2 W 38
Kings Co. Clk's No. 98, Reg. No. 2010
Bronx Co. Clk's No. 5, Reg. No. 8 W 42
Commission Expires March 30, 1942

[NOTARIAL SEAL]

177

178 **Affidavit of Joseph L. Long**

UNITED STATES DISTRICT COURT,
FOR THE SOUTHERN DISTRICT OF NEW YORK.

[SAME TITLE]

STATE OF NEW YORK, }
COUNTY OF NEW YORK, } ss.:

179 JOSEPH L. LONG being duly sworn, deposes and says:

I make this affidavit supplementing my affidavit sworn to September 25, 1941 and attached as Exhibit K to the petition in support of the application to dismiss this proceeding under Chapter X of the Federal Bankruptcy Act. I personally inspected and appraised the premises in question today, September 29, 1941. In my opinion the fair value of the property today is the same as it was on March 15, 1940, when I made my last previous appraisal, to wit, $350,000.00.

JOSEPH L. LONG

180 Sworn to before me this
29th day of September, 1941.

MARGARET ELEANOR WALLING
Notary Public
N. Y. Co. Clk's No. 30, Reg. No. 2 W 38
Kings Co. Clk's No. 98, Reg. No. 2010
Bronx Co. Clk's No. 5, Reg. No. 8 W 42
Commission Expires March 30, 1942

[NOTARIAL SEAL]

Affidavit of Gussie Hammer 181

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK.

[SAME TITLE]

STATE OF NEW YORK, }
COUNTY OF NEW YORK, } ss.:

GUSSIE HAMMER, being duly sworn, deposes and says: 182

I am the president of the debtor herein, and the owner of all of its issued and outstanding stock.

I have read the petition of the Mortgage Corporation of New York. This affidavit is made for the purpose of opposing the granting of the relief as therein prayed for.

DISCUSSION OF PETITION

This petition is very bulky, and, in appearance, formidable. Stripped of its exhibits, however, and boiled down to its essence, it recites but one fact, namely—that in Kings County this petitioner instituted an action against the debtor to foreclose a mortgage, and that such action is still pending, 183 for which reason this court should undo its own order and dismiss this proceeding.

The petition itself contains only seven (7) paragraphs, most of which sounds like a history-book. Paragraphs 1, 2, 3, 4 and 5 relate the past history of the debtor and of the petitioner's relation to it. None of it is new, because it was set forth in the original petition filed by the debtor. This new petition merely repeats and reiterates, in broader form perhaps, and with considerably more detail, all of the allegations contained in my affidavit and the debtor's original petition, upon which two instruments, this proceeding was instituted. Thus although nothing controversial has been

184 *Affidavit of Gussie Hammer*

inserted in these five (5) paragraphs, neither has there been discovered anything new or unknown.

In paragraph 6, however, various new facts, under the title of

"Negotiations for the further reorganization of the mortgage"

are recited. None of these new facts have been heretofore related to this Court. That it was unnecessary to relate "negotiations" is obvious on its face. However, if "negotia-
185 tions" are to be disclosed, then by all means let's have all of them. This, I propose to do later on in this affidavit.

Paragraph 7 adds additional facts, not presently known to this Court, the importance or relationship of which to this proceeding is very doubtful. All that paragraph 7 does is point out that the debtor is in financial distress. I do not dispute this.

This is the petition upon which the Mortgage Corporation of New York seeks to have this Court invalidate this proceeding on the ground that the debtor's petition was not filed in good faith.

NEW FACTS

186 First: Before this proceeding, and even the foreclosure proceeding was instituted, the debtor made every attempt to reorganize its relationship with the certificate holders. Every attempt to do so, however, was severely rebuffed by this very petitioner. Every offer of settlement was brusquely rejected. I sincerely believe that if I could take my proposition to the certificate holders directly, a workable plan, satisfactory to all parties could be obtained. But this opportunity has been denied to me by this very petitioner who has refused any bit of information regarding the certificate holders, except to say that my propositions were unacceptable. An idea can be obtained of the nature of the treatment the debtor received from the petition itself

which speaks of debtor's various offers being "turned down". Everything offered was "turned down", summarily, brusquely, severely and without recourse.

Second: Petitioner speaks of an offer made by the debtor which the petitioner "turned down". The petitioner does not know, nor could it know, that even if the offer had been accepted, the debtor would have been compelled to withdraw it. The offer, when made, contemplated the introduction of new capital funds into the debtor. Counsel for the debtor, when the matter was discussed with them and its aspects analysed, advised us against it, because within a few 188
weeks, the debtor would find itself back in the same situation with identical difficulties. It was therefore compelled to withdraw the offer, but in view of its earlier rejection by this petitioner, the withdrawal became unnecessary.

This situation is well known to the petitioner who, in its own petition, states that on October 1, 1941, approximately $15,000.00 in additional liabilities will accrue against the debtor, and—there are no funds to meet it.

Third: I have been informed, and I do sincerely believe, that the actual cash-realizable-value of the debtor's property is substantially less than its value even as conceded by the petitioner. Some idea can be gleaned of this value from the 189
fact, (and I am informed that it is the actual fact) that the market value of the certificates is approximately 50% of par.

The debtor's plans of reorganization, as they are being presently worked out, contemplate payment to the certificate holders of 100% of their claims.

Fourth: There are junior lienors who have claims against the debtor, as well as its property. Their names, and the nature of their claims, is more particularly set forth in the petition. However, their existence has been ignored and totally disregarded by this very petitioner, not only in this petition, but in the foreclosure proceedings instituted by it.

To treat with these junior lienors, whose claims against the debtor are of equal validity as the certificate holders,

excepting for the security thereof; is the intention of the debtor The court will please rely upon this representation as a statement of absolute truth. In the foreclosure proceedings, even if properly begun, treatment with these junior lienors could not be had. Nowheres, except in this Court, and in a proceeding such as this,—could such dealings and treatment be had.

DEBTOR'S INTENTIONS

This proceeding has been commenced for the sole purpose of effectuating a plan of reorganization with all creditors,
191 in the only court where same is possible. The plan will be founded upon the introduction of new and additional capital funds into the debtor. This, I respectfully submit, is the utmost of good faith, in fact, its actual definition and the essence of its meaning, as Congress must have intended it when enacting the Bankruptcy Act.

I sincerely believe that I can effectuate such a plan, provided that the rights afforded to me by law are fully protected. This petitioner, if it be permitted to go through with its intentions, will succeed in denying those rights to the debtor. In this Court, where I can deal directly with the owners of the certificates, I am sure some plan,—fair, equitable and feasible,—will be worked out and ratified. For
192 the certificate holders, in the last analysis are the real and actual creditors, the ones who must ultimately and finally pass upon any proposed plan. For this opportunity, I earnestly pray this Court.

GUSSIE HAMMER

Sworn to before me this
29th day of September, 1941.
SOL FRIEDLAND
Comm. of Deeds
N. Y. City
Exp 2/4/43

193

Affidavit of Samuel Silverman

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

[SAME TITLE]

SOUTHERN DISTRICT OF NEW YORK }
STATE OF NEW YORK } ss.:
COUNTY OF NEW YORK }

194

SAMUEL SILVERMAN, being duly sworn, deposes and says:

I am one of the Trustees of the Debtor heretofore appointed by this Court, by its Order of September 17th, 1941, wherein it approved the Debtor's petition for relief pursuant to the provisions of Chapter X of the Bankruptcy Act (hereinafter referred to as the Chandler Act), and assumed jurisdiction over the Debtor and its property. My appointment as such Trustee was made on the Debtor's petition that I be appointed as an additional Trustee, as provided for in Section 156 of said Chandler Act, having heretofore been associated with the Debtor as its Vice President and General Counsel.

195

The Debtor's petition herein was filed with my full approval. The decision so to invoke the jurisdiction of this Court was arrived at only after a careful analysis of the Debtor's structure and financial problems, and was the result of a firm conviction that only by availing itself of the beneficent provisions of the aforesaid Chandler Act, could the Debtor obtain adequate relief for itself, and a definitive solution and liquidation of its creditors'—(both secured and unsecured)—interests.

Viewing the problem from the vantage point of retrospect and in the light of what is affirmatively alleged in the instant

moving petition of the MORTGAGE CORPORATION OF NEW YORK, the first Mortgage Indenture Trustee, but confirms my prior conclusions that it is only in this Forum, and under the all comprehensive scope and basic philosophy of the aforesaid Chandler Act, that complete equity and practical justice could be achieved in the adjustment of the Debtor's interest *vis a vis* its unsecured creditors and the respective classes of its security holders and lienors.

In the hope that I might be of assistance to the Court in its determination of the instant application, I respectfully submit this affidavit and accompanying Memorandum of Law,
197 not as a partisan advocate of a limited interest, but as a Trustee and officer of this Court, with all the conscious objectivity and detachment which the Court's designee should at all times observe in the discharge of the trust reposed.

Towards the close of August, 1941, I was advised by Mr. & Mrs. Hammer, my fellow officers in the Debtor Corporation, that they had succeeded in procuring additional financing in a sum approximately $7,500, which sum, added to the net balance remaining in the hands of Mr. Rubenstein, the Receiver in foreclosure, after payment of the Receiver's and his Counsel's fees, would enable the Debtor to cure the defaults constituting the basis of the foreclosure proceedings,
198 and thus procure a discontinuance thereof.

I pointed out that their plan was but a stop-gap, and did not touch the heart of the problem; that in October, 1941, an additional $15,000 would accrue and become payable as and for interest on the first mortgage and current real estate taxes, which sum, I knew, they would be unable to obtain, thereby precipitating again another foreclosure of the first mortgage; that the first mortgage affecting the premises was more than six times the annual rental reserved or actually received, whereas the normal first mortgage affecting premises such as the property of the Debtor, at this time, does not exceed three to three and a half times the

annual rental reserved; that no provisions were being made either for the junior lienors or for unsecured creditors, and that the vicious cycle of an overburdened and topheavy financial structure, and the feverishly frantic efforts to forestall and stave off disaster would continue, with an inevitable and unavoidable collapse as the ultimate certainty; that unless a fundamental revision of the Debtor's capital structure could be achieved, with the consent of all creditors, secured and unsecured, either by immediate satisfaction on the basis of actual rather than formal value, or a long range plan of equitable liquidation, it was utterly impossible ever to see the end of the road. 200

We then considered the practical possibilities of such a workable plan of reorganization as well as the best methods and avenues of accomplishing such desired end. It became clear at once, and I so advised my client, that no adequate relief could be obtained by any known proceedings, equity or otherwise, in our State Courts.

In the first place, the Schackno Act, under which the Supreme Court of New York assumed jurisdiction over the first mortgage affecting Debtor's property, only related to supervision over and reorganization of certificated first mortgage issues, and properties of Mortgage Corporations or institutions in process of reorganization. It had no relation to and concerned itself little, if any, with the problem of junior lienors, and the equities between such different classes of security holders, the problem of unsecured creditors, or that of the owner of the property itself. 201

Secondly, our experience in broaching the subject of reorganization of the first mortgage indicated that no possible solution could be obtained by resort to the State Court. The Mortgage Corporation, Indenture Trustee, interposed itself as a non-conductor preventing direct contact between the debtor and the certificate holders who are the real parties in interest, so far as the reorganization of this first mortgage

is concerned. I pointed out to my client that this property was then entering its second decade of existence, a period during which, according to universal experience, there was not only an increased operating and maintenance cost, but also increased capital replacement requirements; that the insistence of the Mortgage Corporation upon the use of the entire income of the property for payment of interest on the first mortgage and a nominal amortization, without providing for any reserve of any part thereof, either in the form of return upon the Debtor's investment or for the partial satisfaction of junior liens, and without providing for a
203 reserve to meet the increased cost of operation and the probable capital replacement needs, as a condition precedent to its entertaining a plan or reorganization for the submission to the Certificate Holders for their decision, rendered futile any plan or any idea of obtaining practical results from that medium.

I therefore advised recourse to this Court under the provisions of the Chandler Act, where complete relief could be obtained and a workable plan evolved as the only method of solution of the Debtor's quandary. We considered possible plans for ultimate submission to the Court, and, through the Court, to all creditors. I was assured by my client, and an independent investigation convinces me that their assurances
204 were not a figment of imagination, that if the creditors desire liquidation of their claims on the basis of present actual values rather than on the face amount of their claims, such results could be achieved by refinancing the first mortgage on the property and placing thereon a new institutional first mortgage, and the addition of about $50,000 in cash. The sum which, we felt, we would realize from such a plan would be sufficient to pay certificate holders of the first mortgage alone a sum in excess of that which would be realized by their sale of their certificate in the open market, or that which they would realize by retaining their lien on the property

with its increasing depreciation, as well as take care of the other creditors. On the other hand, if the creditors preferred gradual liquidation of their claims in the full amount, a long range plan was feasible whereby the interest rate was to be reduced substantially and increased amortization made on account of such creditors' claims.

I know that the petition of the debtor was filed in good faith and not for delay, with the hope of evolving a reorganization plan deemed equitable by the Court and acceptable in fact to all of the creditors. As a Trustee, I am satisfied, and I express it as my opinion, that such a plan would in the long run even be more beneficial to the certificate holders of the first mortgage themselves, and would be the only means whereby the other creditors of the Debtor, junior lienors and unsecured creditors, as well as the Debtor itself would obtain some measure of relief. 206

SAMUEL SILVERMAN

Sworn to before me this
29th day of September, 1941.

BEATRICE U. KANE
Notary Public, Bronx County
Bronx County Clerk's No. 153
New York County Clerk's No. 607
Commission Expires March 30, 1943 207

208 **Opinion of District Court**

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE]

BRIGHT, *D. J.*

HUGHES, HUBBARD & EWING, ESQS.,
By CURTISS ELY FRANK and ORVILLE H. SCHELL, JR., ESQS., Of Counsel, Attorneys for The Mortgage Corporation of New York,
209 1 Wall Street, New York City.

FRIEDLAND & FRIEDLAND, ESQS.,
By ARTHUR E. FRIEDLAND, ESQ., Of Counsel, Attorney for Debtor,
291 Broadway, New York City.

GEORGE ROSLING, ESQ.,
Attorney for Mortimer Rubenstein as Receiver.

SAMUEL SILVERMAN and MAURICE RUBINGER, ESQS.,
Trustees, In person.

210 This is an application by The Mortgage Corporation of New York as trustee, to vacate an order made herein on September 17th, 1941 approving the petition of the above named debtor, filed for reorganization under Chapter X of the Bankruptcy Act (Title 11 U. S. C. A. Sections 501-672), under which trustees have been appointed and qualified, and to dismiss such petition. The ground of attack mainly is that the petition for reorganization was not made in good faith.

It appears without dispute that the secured indebtedness of the debtor consists of a first mortgage held by The Mortgage Corporation, amounting, with defaults as of October

1st 1941, to $399,814, of a second mortgage of $25,000, of a third and fourth mortgage upon each of which there is due not more than $2,000, and conditional sales contracts aggregating about $3,000, a total of $431,814; and there is unsecured indebtedness, the amount of which is not disclosed. The value of the real estate concededly does not exceed $350,000, it being assessed at $380,000.

The first mortgage was originally given to the Title Guarantee & Trust Company, and certificates were issued under it to about ninety holders, which certificates were guaranteed by the Bond & Mortgage Guaranty Company. The latter company becoming insolvent, its affairs were taken over by 212
the New York Superintendent of Insurance, and the mortgage in question was reorganized under the New York Schackno Act, the plan being approved by the New York Supreme Court in Kings County, on November 24th 1934, and declared final on December 6th 1934, after approval by two-thirds in amount of the certificate holders. Under that plan, the mortgage was extended for three years to December 1st 1937, with interest at 6% to December 1st 1934, and thereafter at 5% to maturity.

Subsequently, The Mortgage Corporation was appointed, and is now acting as trustee pursuant to an order of the State Court, made December 6th 1938, which order further pro- 213
vided that the court should retain jurisdiction of the proceeding until the complete liquidation of the trust estate.

The first mortgage was not paid at its maturity, and on April 1st 1941, the debtor defaulted in the payment of interest and taxes; on May 1st, 1941, foreclosure proceedings were begun in the State Court, and are now pending, in which action a receiver was appointed, who took possession of the property, and has since been collecting the rents therefrom and operating the same.

Negotiations for a further modification of the mortgage attempted on two occasions by the debtor, in which further extension of payment and reduction in interest were sought,

were unsuccessful, The Mortgage Corporation declining each after submitting the same only to its Trust Committee. No submission of the proposed modification was made either to the court or to the certificate holders. The receiver estimates that the property is capable of earning approximately 6⅔% upon the first mortgage, and upon the argument, it was stated by his attorney that there was but one vacancy in the premises.

In opposition to the application, it is shown that the market in New York City for certificates issued under the first mortgage in question, is, at present, 50% of par; and
215 it is contended that the reorganization in the State Court can only affect the certificate holders under the first mortgage, and cannot take into consideration the subsequent liens, as well as the unsecured creditors.

The decline in the value of the real property, the fact that the value of the certificates in the market is so much less than par, and the power of this court in any attempt to reorganize to consider the rights of all lienors and creditors, as seems to be the purpose of the Chapter X of the Bankruptcy Act, convinces me that the application now made should be denied, and to require a finding that the original petition was filed in good faith. Certainly, the object of the
216 Chapter is to make a fair and equitable application of the assets of the debtor, which cannot meet its obligations by payment in full as they mature, to an adjustment of its debts. Such an object cannot be attained in the State Court proceeding. It may be here. What plan may be presented cannot now be definitely ascertained. The Chapter contemplates an opportunity on the part of the trustees in reorganization to present one, and certainly does not contemplate a reorganization for the sole benefit of any particular creditor, secured or otherwise. It does not provide for a dismissal of such proceeding because a single creditor opposes it, nor because such creditor contends that no plan can be presented.

If the first mortgage creditor is to be given a free hand, it is obvious, in view of the present depreciated value of the real estate, that not only will all creditors be wiped out, but also that the certificate holders will receive only a fraction of their investment. Can those certificate holders fare any better after a forced sale of the real estate than in this proceeding? There seems to be no question but that the debtor should be reorganized. The question is whether that should proceed in this court, where all creditors may be heard, or in the State Court, which has control over but one class of creditors. I do not think the time has yet arrived to 218
decide that question, nor can it arrive until an opportunity has been given to learn what kind of a plan can be presented. At present but one creditor is being considered, and its foreclosure has been pending for four months without any apparent progress being made.

Four cases in this district seem to have marked out the bounds within which this application may be considered. In Brooklyn Trust Co. v. Rembaugh, 110 F. 2d 838, the Circuit Court of Appeals for the Second Circuit, reversed an order denying an application similar to this where the facts were almost parallel. No doubt was there found as to the jurisdiction of the District Court, nor, it was written, any substantial ground for attacking the exercise by the trial 219
judge of discretion in approving the petition as filed in good faith within the broad meaning of that term. But it was there held that the debtor, after assenting to the plan in the State Court, could not escape from the consequences of the plan simply by filing a petition for reorganization in the Federal Court, while proceedings in the State Court were still pending. The distinction between that case and this, it seems to me, is that here the debtor has endeavored on two occasions to present modified plans for relief, but on each occasion, has been rebuffed by the trustee, and has had no opportunity to make application for the relief which obviously the situation requires. The Act, I think, contemplates

the right on the part of the debtor to go to the certificate holders direct, for otherwise, I cannot see the reason for Section 565 of Title 11 U. S. C. A.

In Castle Beach Apartments, 113 F. 2d 762, an order denying a motion similar to this was affirmed, and the facts there were quite similar, except that the debtor there had not been a party to any reorganization plan in the State Court; but citing Brooklyn Trust Co. v. Rembaugh, supra, it was held that if it had that alone would not have been adequate ground for a dismissal of the petition. The fact that 75% of the certificate holders indicated in that case
221 that they would not approve any plan was no proof that such an expression of disfavor was obtained with the consent of the court pursuant to law. I think the inference is that those most interested should have the right to say whether or not the plan to be proposed would be satisfactory. It was further stated that there was no sufficient reason because the debtor might be shown to be insolvent, for deciding that the District Judge did not exercise sound discretion in approving the petition and refusing to dismiss; that it could not be said that the attempt to reorganize was so hopeless that good faith was absent.

In Blinrig Realty Corp., 114 F. 2d 100, the order ap-
222 proving the petition filed under Chapter X was reversed. It was there said that good faith in the sense of a fair likelihood of success, in view of the vain efforts to reorganize already made in the State Court, were needed to be shown prima facie at least in order to entitle the petition to approval. The efforts made by the debtor there were obviously unfruitful, so much so, that the court concluded that there was no reasonable ground for believing that the debtor's creditors would agree to a plan with less favorable terms, or that the debtor could do any better in the proceeding under the Federal Act, than it had in the State Court.

There has obviously been no fair effort here to determine any such a thing. Each suggestion made by the debtor

has gone no further than the Trust Committee of The Mortgage Corporation. What the creditors might do, particularly in view of the fact that certificates are selling at one-half their face value, and that the property is worth less in the market than the first mortgage, is most problematical. Consideration should be given to the possibility that new money may enter the picture, which prospect can be probed by any plan which the trustees may propose.

And, lastly, In re 263 West 38th Street Corporation, 37 F. Supp. 667, an order for reorganization was approved by Judge Hulbert in an opinion in which the foregoing cases were cited and discussed, and in which he wrote that no 224
indication having been given with respect to the contemplated terms of reorganization, whether a plan could be prepared and submitted which would be fair, feasible and equitable, could best be determined after a hearing.

I think that under all the circumstances shown here, the trustees should be given an opportunity to submit such a plan, and that the application of The Mortgage Corporation should be denied. (In re Mt. Forest Fur Farms, 103 F. 2d, 69; cert. denied 308 U. S. 583.)

Upon the argument, the receiver's counsel requested that if the application were denied, he be permitted to retain some amount of money as a possible backlog against the 225
payment of his commissions and his attorneys' fees. I do not think that is necessary. The order to be entered upon this motion can provide that the turning over by him of such moneys which he has in his possession, and his subsequent accounting, shall be without prejudice to his application for commissions and attorneys' fees.

Application denied. Settle order on notice.

Dated: N. Y. September 30th 1941.

(sgd) JOHN BRIGHT
U. S. D. J.

226 **Petition of Marine Harbor Properties, Inc.**

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK.

[SAME TITLE]

To the Honorable Justices of the District Court of the United States, for the Southern District of New York:

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The petition of Marine Harbor Properties, Inc., hereinafter referred to as the "debtor", pursuant to Chapter X of "An Act to Establish a Uniform System of Bankruptcy Throughout the United States," approved June 22, 1938, and acts amendatory thereof, respectfully alleges:

1. The debtor herein is a corporation duly organized and existing under and by virtue of the laws of the State of New York, and is not a municipal, railroad, insurance, or banking corporation, or a building and loan association.

2. The debtor's principal place of business is c/o Olesker, 228 570 Seventh Avenue, in the Borough of Manhattan, City and State of New York, and during the six months immediately preceding the filing of this petition, and prior thereto, the debtor had, and now has, its principal place of business in the Southern District of New York.

3. The debtor is engaged in the business of owning and operating real estate and has been so engaged since its organization on February 10, 1933.

It is now the owner of a parcel of real property situated in the County of Kings, State of New York, and being described as follows:

All that lot or parcel of land, with the buildings and improvements thereon, in the Borough of Brooklyn, County of Kings, City and State of New York, bounded as follows:

BEGINNING at the corner formed by the intersection of the Northeasterly side of Marine Avenue and the northwesterly side of Fourth Avenue (100 ft. wide) running thence northeasterly along the northwesterly side of Fourth Ave., (100 ft. wide) one-hundred and fourteen feet and five and one-half (114-5½") inches, thence northeasterly parallel with Marine Avenue, 230
139 ft.; thence northeasterly parallel with Fourth Avenue, 7 ft. 6½", thence northwesterly with Marine Avenue, 75 ft.; thence southwesterly and at right angles to Marine Avenue, 122 ft. to the northeasterly side of Marine Ave., thence southeasterly along the northeasterly side of Marine Avenue, 214 ft. to the point or place of beginning, said premises being known as 351 Marine Avenue.

4. The aforesaid property, owned by the debtor, is subject to four open mortgages.

(a) One of the said mortgages was made by Marine Building Corp. to secure the payment of the principal sum 231
of $370,000 to Title Guarantee & Trust Co. with interest thereon. Said mortgage was dated on or about April 28, 1931, and was recorded on April 28, 1931, in the Office of the Register of the County of Kings, in liber 7634 of Mortgages, at Page 128.

The property aforesaid, originally owned by Marine Building Corp. was by deed, (recorded in the Office of the Register of the County of Kings, on September 10, 1931,) conveyed to Marine Holding Corp., which corporation in turn, by deed (recorded in the Office of the Register of the

232 *Petition of Marine Harbor Properties, Inc.*

County of Kings on February 20, 1933), conveyed the aforesaid property to petitioner. All of the aforesaid conveyances were made subject to the original mortgage given to the Title Guarantee & Trust Co.

Title Guarantee & Trust Co. issued certificates of participation against said mortgage, constituting assignments of parts of the said mortgage, and these were issued to approximately 90 persons, all hereinafter referred to as the certificate holders. Bond & Mortgage Guarantee Co. guaranteed the payment of the interest on and the principal of said cer-
233 tificates to the certificate holders.

The aforesaid mortgage in the sum of $370,000 was modified by agreement between petitioner and Title Guarantee & Trust Co. on March 11, 1935. Said agreement provided that the date of the payment of the principal sum of $370,000 be extended to December 1, 1937, upon condition that petitioner pay interest at 5% per annum, beginning April 1, 1935, and semi-annually thereafter; this extension agreement was made pursuant to an order of the Supreme Court of the State of New York, County of Kings, dated December 6, 1934.

Bond & Mortgage Co., aforesaid, having become insolvent, a proceeding was instituted for a readjustment of the rights
234 of the certificate holders under Chapter 746 of the Laws of 1933, as amended, in the Supreme Court of the State of New York, County of Kings, and a final order was entered therein, on the 6th day of December, 1938, appointing the Mortgage Corporation of New York, trustee of the said issue, and the said Mortgage Corporation of New York, since the making and entry of the aforesaid order, has been acting as such trustee.

All of the terms and conditions of the said bond and mortgage, as modified by the aforesaid extension agreement, have been fully complied with except:

1. That the principal of the said mortgage, which became due on December 1, 1937, under the terms of the said extension agreement, has not been paid.

2. That the interest due on said mortgage on April 1, 1941, has not been paid.

3. Taxes due the City of New York, on April 1, 1941, on the assessed valuation of said property have not been fully paid.

236 The debtor is not liable upon the bond, secured by the mortgage hereinbefore referred to.

(b) The second mortgage, also encumbering the property of the debtor, is owned by Friedwald Mortgage Corp. of 7321 Fifth Avenue, Brooklyn, New York. Said mortgage was recorded on December 10, 1930, in the Office of the Register of the County of Kings, in liber 7350, page 334 of Mortgages. It was made to secure the payment of the principal sum of $82,750, and when originally made, it was a first lien on the aforesaid property. However, by agreement dated May 1, 1931, the aforesaid mortgage was subordinated to the mortgage in the sum of $370,000 hereinbefore more 237 particularly described, and presently remains a second lien on the property herein. The balance due on this mortgage is $25,000.00.

(c) In addition to the foregoing mortgages, there is a third mortgage made to Max Olesker and Morris Aronson, in the principal sum of $8,724.07, recorded on November 2, 1938, in the Office of the Register of the County of Kings, in Liber 8286, Page 530 of Mortgages. There is a dispute as to the principal amount now due on said mortgage, but same does not exceed the sum of $2,000.00.

238 *Petition of Marine Harbor Properties, Inc.*

(d) In addition, there is a fourth mortgage made to Joseph Schwartz, recorded on November 4, 1940, in the office of the Register of the County of Kings in Liber 8617, Page 6, made to secure payment of the principal amount of $8,480.60. There is a dispute between the debtor and the mortgages as to the principal amount now due, but same does not exceed $2,000.00.

(e) The property owned by the debtor is also subject to various other mortgages of record, all of which have been paid, and for which satisfaction pieces are in the possession
239 of petitioner or its representatives. None of these mortgages, however, have been discharged as of record in the Office of the Register of the County of Kings, because of failure of funds to accomplish same.

(f) The property owned by the debtor is also subject to various conditional bills of sale affecting refrigeration fixtures installed in the premises of the debtor. The balance due on the purchase price thereof is approximately $3,000.00, and the conditional bills of sale remain unsatisfied because thereof. In all cases, the conditional vender is the Kings Appliance Corp.

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5. That there are no proceedings pending against the debtor or affecting its property excepting that commenced by the Mortgage Corporation of New York, on or about the 3rd day of May, 1941. This proceeding was commenced for the purpose of foreclosing the first mortgage hereinbefore more particularly described. Said proceeding is presently pending in the Supreme Court of the State of New York, County of Kings, and is entitled as follows:

THE MORTGAGE CORPORATION OF NEW YORK, as Trustee under a declaration of trust, dated December 12, 1938, executed pursuant to a plan of readjustment, etc., of the rights of the holders of investments in a certain mortgage covering premises 351 to 363 Marine Ave., Borough of Brooklyn, County of Kings, City and State of New York, guaranteed by Bond & Mortgage Guarantee Company, Guarantee No. 181,368, approved by a final order of the Supreme Court of the State of New York, for the county of Kings, entered the 6th day of December, 1938, and for the benefit of the holders of investments in said mortgage, 242

Plaintiff,

against

MARINE HARBOR PROPERTIES, INC. MARINE BUILDING CORPORATION, LOUIS H. PINK, Superintendent of Insurance of the State of New York, as Liquidator of Bond and Mortgage Guarantee Company, and as successor to Mortgage Commission of the State of New York, as successor to and assignee of certain liens of Mortgage Commission of the State of New York, and THE PEOPLE OF THE STATE OF NEW YORK, 243

Defendant.

6. That simultaneously with the commencement of, and in, the aforesaid proceeding Mortimer Rubenstein, was duly appointed receiver by the Supreme Court of the State of New York, County of Kings. He immediately entered into possession of the premises owned by the debtor and is presently acting as receiver of its property.

244 *Petition of Marine Harbor Properties, Inc.*

7. The assets, liabilities, capital stock and financial condition of the debtor, as of September 15, 1941, are as follows:

ASSETS: The debtor has no cash and no assets other than the property above referred to, and now in the possession of Mortimer Rubenstein, as receiver. The income from the property above referred to, is likewise in the hands of the said Mortimer Rubenstein, as receiver. Such income is sufficient to meet the interest on the mortgages affecting petitioner's property, or allocable to it, but it is insufficient to
245 enable it to pay the principal amount of said mortgage.

LIABILITIES: The debtor owes approximately the following amounts:

(a) $370,000 principal due on the first mortgage above described, with accummulated interest thereon.

(b) $25,000 on the second mortgage above described.

(c) A sum, not in excess of $2,000, due on the third mortgage, above described.

(d) A sum, not in excess of $2,000, due on the
246 fourth mortgage, above described.

(e) $3,000 balance due for refrigeration assets purchased on conditional bills of sale.

(f) and is indebted to its counsel for legal services rendered and to be rendered in connection with this and other proceedings, looking to the reorganization of the debtor.

(g) Such amounts as may be due the State of New York, for possible franchise taxes as well as any other taxes.

(h) Unknown amount due unsecured creditors, for current expenses incurred just previous to the institution of the foreclosure proceedings above described. The exact names, addresses and amounts of claims of said creditors are unknown to petitioner.

That, upon information and belief, none of the unsecured creditors of the debtor, excepting the State of New York, and Friedland & Friedland, Esqs., holds a claim in excess of 5% of the total of all claims.

That there are no secured creditors of the debtor other than the holders of the securities above set forth. 248

CAPITAL STOCK: The capital stock of the debtor consists of 100 shares each of the par value of $100.00, all common stock, and all of which is issued and outstanding.

FINANCIAL CONDITION OF THE DEBTOR: The financial condition of the debtor is as hereinbefore set forth.

8. The debtor is unable to meet his debts as they mature and desires to effect a plan of reorganization pursuant to Chapter X of the Chandler Act. Its liabilities exceed in amount $250,000. 249

9. That there is pending no plan of re-organization, readjustment, or liquidation affecting the property of the debtor, either in connection with, or without, any judicial proceeding.

10. A plan for the re-organization of the debtor is now being formulated. It will provide for a revamping of the debtor's corporate structure and of its secured indebtedness. Adequate relief under Chapter XI cannot be obtained, because Chapter XI affects only unsecured indebtedness.

11. The debtor presently situated, is unable to secure additional capital, but has received assurances that, if a satisfactory re-organization is consummated under Chapter X and as part thereof, additional capital funds will be made available.

12. The filing of this petition by the debtor has been duly authorized by resolutions of the Board of Directors adopted at a meeting thereof, held on September 10, 1941, as shown by the certificate of the debtor marked Schedule "A", and made a part hereof.

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13. The purpose of this proceeding is to procure a readjustment of the corporate structure, and all its secured indebtedness, so as to extend the time of payment of said secured indebtedness, upon such terms as will enable the debtor to pay a reasonable amount annually in reduction of the principal thereof in accordance with the provisions of a plan of re-organization to be presented to this Court.

14. That no previous application, by or in behalf of the debtor has been made to this Court or any other Court for the relief as prayed for herein.

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Wherefore, the debtor prays that this Court enter an order granting the following relief:

(1) Finding that this petition complies with, and is properly filed under, Chapter X of the Bankruptcy Act.

(2) That the debtor is unable to meet its debts as they mature.

(3) That said petition has been filed in good faith.

(4) Appointing a trustee to take possession of the property and assets of the debtor.

(5) Appointing SAMUEL SILVERMAN, a director of the debtor and an officer thereof, to wit: Vice-President, as an additional trustee, in accordance with Section 156 of the Bankruptcy Act.

(6) Enjoining and restraining the debtor, its stockholders, directors, officers, superintendents, managers, attorneys, agents, employees, and creditors, their agents and employees, and all other persons, firms or corporations, including Sheriffs, Marshals or other officers, agents, attorneys, representatives, servants or employees, whether same are creditors or 254
claiming to be creditors, or having or claiming to have any right, title and interest in and to the property of the debtor, from interfering with, transferring, selling, or disposing of, any of the property or income constituting the debtor's estate and from the commencement or continuing of any suit or suits against the debtor until a final decree in this proceeding has been made and from levying any attachment, execution or other process upon or against any of the properties constituting the debtor's estate and from doing any act whatsoever to interfere with the possession, operation, or management by the trustees, of the property, and business constituting the debtor's estate, or 255
interfering in any way with the trustees, in the discharge of their duties or interfering in any way with the administration or disposition of the affairs and properties constituting the debtor's estate.

(7) Reserving full right and jurisdiction to make from time to time, such orders as to this Court may seem proper, fixing time within which any plan of reorganization may be proposed, accepted, or confirmed, requiring to be filed such schedules and information as may be necessary in this proceeding, the

256 *Petition of Marine Harbor Properties, Inc.*

division of creditors into classes, and in general such order carrying out, amplifying, extending, limiting, or otherwise modifying the order as to this Court may seem just and proper at any time.

(8) Granting such other, further and different relief as to this Court may seem just and equitable in the premises.

Dated: New York, September 15th, 1941.

257 MARINE HARBOR PROPERTIES, INC.

By: .....
President.

FRIEDLAND & FRIEDLAND
Attorneys for Debtor
Office & P. O. Address
291 Broadway
Borough of Manhattan
City of New York.

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STATE OF NEW YORK,
COUNTY OF NEW YORK, } ss.:

GUSSIE HAMMER, being duly sworn, deposes and says: That she is the president of the MARINE HARBOR PROPERTIES, INC. That she has read the foregoing petition and knows the contents thereof; that the same is true to her own knowledge, except as to the matters therein stated to be alleged on information and belief, and that as to those matters, she believes it to be true.

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GUSSIE HAMMER

Sworn to before me this
15th day of September, 1941.

MIRIAM HARMALIN
Notary Public
Com. exp. Mar. 30/42.

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EXHIBIT "A", ANNEXED TO PETITION OF MARINE HARBOR PROPERTIES, INC.

I, GUSSIE HAMMER, Secretary of MARINE HARBOR PROPERTIES, INC., a New York corporation, DO HEREBY CERTIFY, that I am the Secretary of said Corporation and that at a meeting of the Board of Directors duly convened and held on September 10, 1941, at which meeting a quorum was present, the following resolutions were adopted:

RESOLVED: That this corporation file a petition for re-
263 organization under and in pursuance of Chapter X of the Bankruptcy Act of 1939, as amended; and it is further

RESOLVED: That the proper officers of this corporation be, and they hereby are, authorized and empowered to execute such petitions and other instruments, and to take or cause to be taken such proceedings as may be necessary, or desirable to secure to this corporation any and all relief in pursuant of Chapter X of the Bankruptcy Act of 1939, as amended.

I DO FURTHER CERTIFY that such resolutions are in full force and effect.

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IN WITNESS WHEREOF, I have hereunto set my hand and the seal of the corporation, this 10th day of September, 1941.

GUSSIE HAMMER (L. S.)
Secretary

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Affidavit of Gussie Hammer, Submitted with Debtor's Petition

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

IN THE MATTER

of

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MARINE HARBOR PROPERTIES, INC.,

Debtor.

STATE OF NEW YORK,
COUNTY OF NEW YORK, } ss.:

GUSSIE HAMMER, being duly sworn, deposes and says:

I am the president and secretary of the MARINE HARBOR PROPERTIES INC., the above named debtor. This affidavit is 267
presented with a petition for reorganization of the debtor, pursuant to rule X-4 of the Rules of the United States District Court, for the Southern District of New York.

A) There is no action or proceeding in rem pending or threatened against the debtor's property, excepting an action to foreclose the first mortgage. Same is pending in the Supreme Court of the State of New York, and is entitled as follows:

268 *Affidavit of Gussie Hammer, Submitted with Debtor's Petition*

THE MORTGAGE CORPORATION OF NEW YORK, as Trustee under a declaration of trust, dated December 12, 1938, executed pursuant to a plan of readjustment, etc., of the rights of the holders of investments in a certain mortgage covering premises 351 Marine Avenue, Brooklyn, County of Kings, City and State of New York, guaranteed by Bond & Mortgage Guarantee Company, Guarantee No. 181,368, approved by a final order of the
269 Supreme Court of the State of New York for the County of Kings, entered the 6th day of December, 1938, and for the benefit of the holders of investments in said mortgage,

Plaintiff,

against

MARINE HARBOR PROPERTIES, INC., MARINE BUILDING CORPORATION, LOUIS H. PINK, Superintendent of Insurance of the State of New York, as Liquidator of Bond and Mortgage Guarantee Company, and as successor to Mortgage Commission of the State of New York, MORRIS S. TREMAINE, Comptroller of the State of New York, as
270 successor to and assignee of certain liens of Mortgage Commission of the State of New York, and THE PEOPLE OF THE STATE OF NEW YORK,

Defendants.

There are no actions or proceedings in personam pending or threatened against the debtor in which a judgment against the debtor or seizure of its property may be imminent, excepting that on June 2, 1941, Seaberg Elevator Co., Inc., perfected and docketed a judgment in the Office of the Clerk of the County of Kings, in the sum of $250.09, which was

Affidavit of Gussie Hammer, Submitted with Debtor's Petition 271

recovered in the Municipal Court of the City of New York, Borough of Brooklyn, First District.

B) 1. That there are no issues of outstanding bond debentures, or other evidences of indebtedness of the debtor, secured by or issued under an indenture or other similar instrument, excepting an extension agreement mentioned in the petition herein.

The original mortgage had been made by debtor's predecessor-in-interest and the debtor has acquired title to its property subject to the aforesaid mortgage. 272

As pointed out in the accompanying petition, the certificates of participation in the first mortgage of $370,000, covering the debtor's property were issued to the general public by Title Guarantee & Trust Co. and guaranteed by the Bond & Mortgage Co., which guaranteed such certificate holders the payment of the principal and interest on said certificates. The certificates of participation were issued against the first mortgage, covering the debtor's property.

Bond & Mortgage Guarantee Co. thereafter became insolvent and a proceeding for the reorganization of the said mortgage under Chapter 745 of the Laws of 1933, as amended, was instituted in the Supreme Court of the State of New York, Kings County. In said proceedings, the Mortgage 273 Corporation of New York was appointed trustee of the said mortgage for the benefit of the certificate holders.

I am informed, and do verily believe that the certificates of participation are held by approximately 90 persons in the United States, both within and without the State of New York. The source of this information is an affidavit of service contained in the records of the Supreme Court of the State of New York, County of Kings.

2. In addition to the foregoing mortgage, certificated as aforesaid, there is a second mortgage covering the property

of the debtor upon which the debtor is also not personally liable. The second mortgagee is the Friedwald Mortgage Corp. of 7321 Fifth Avenue, Brooklyn, New York. It was given by debtor's predecessor-in-interest to secure payment of an original sum of $82,750.00. By agreement with the said mortgagee, made by the debtor, there is presently due on said second mortgage the principal sum of only $25,000.00.

3. In addition to the foregoing mortgages, there is a third mortgage made to Max Olesker and Morris Arenson, in the principal sum of $8,724.07, recorded on November 2, 1938, in the Office of the Register of the County of Kings, in Liber 8286, Page 530 of Mortgages. There is a dispute as to the principal amount now due on said mortgage but same does not exceed the sum of $2,000.00.

4. In addition, there is a fourth mortgage made to Joseph Schwartz, recorded on November 4, 1940, in the Office of the Register of the County of Kings in Liber 6617, Page 6, made to secure payment of the principal amount of $6,480.00. There is a dispute between the debtor and the mortgagee as to the principal amount now due, but same does not exceed $2,000.00.

5. In addition to the foregoing four mortgages, there are various other mortgages still recorded as encumbering the property of the debtor, but all of which have been satisfied and for which satisfaction pieces remain in the possession of the debtor. The satisfaction pieces, for financial reasons, have not been filed and recorded in the Offices of the Register of the County of Kings.

6. That in addition to all of the foregoing, mortgages, there are various conditional bills of sale filed in the Office of the Register of the County of Kings, and encumbering

refrigeration assets, lately installed in the premises of the debtor. In all cases, the conditional vendor is the Kings Appliance Corp. of Brooklyn, New York.

C. The approximate total number of unsecured creditors of the debtor, other than the holders of indebtedness mentioned in subdivision "B" is ten (10), and the name of each creditor, who has a claim against the debtor in excess of 5% of the total of such claim is:

(1) State of New York 278

(2) Friedland & Friedland, Esqs.

There are several other unsecured creditors, whose exact names, addresses, and the amounts due them, are unknown to deponent, because of the fact that the petitioner has been out of possession of the premises and its books for the past several months, since the receiver was appointed, and deponent is unable at the moment, to accurately set forth their exact names, addresses and the amounts due them.

D) The names and addresses of each secured creditor other than the holders of securities specified in subdivision "B)1", the approximate amount of the indebtedness of each, and a brief statement of the nature of the security held by each are as follows: 279

1) Friedwald Mortgage Corp.
8321 Fifth Avenue
Brooklyn, N. Y.

This creditor owns a second mortgage on the property of the debtor. The amount due thereon is $25,000.

2) Max Olesker & Morris Aronson,
570 Seventh Avenue
New York City

280 *Affidavit of Gussie Hammer, Submitted with Debtor's Petition*

This creditor owns a third mortgage on the property of the debtor on which there is a balance due not in excess of $2,000.

3) Joseph Schwartz
570 Seventh Avenue
New York City

This creditor owns a fourth mortgage on the property of the debtor and the amount due thereon is also not in excess
281 of $2,000.00.

B) A brief description of all the property,—in the possession of the debtor, any public officer, receiver, trustee, assignee for the benefit of creditors, mortgages, pledgee, or assignee of rents,—is:

All that part, parcel or piece of land known and described as 351 Marine Avenue, Brooklyn, New York, more particularly set forth in the accompanying petition.

MORTIMER RUBENSTEIN was duly appointed receiver of this property by order of the Supreme Court of the State of New York, County of Kings, in the foreclosure action
282 specified above. He is presently in possession thereof, as such receiver. The property consists of an apartment house, containing approximately 320 rooms, and there has been and still is an annual income in excess of $50,000 from the rental of the aforesaid rooms.

F) A trustee or trustees should be appointed herein by this Court because of the fact that the fixed and liquidated indebtedness encumbering the property of the debtor exceeds in amount $250,000.00. Accordingly, in addition to the trustee to be appointed by this Court, an additional trustee may be appointed herein in accordance with Section 156 of the

Affidavit of Gussie Hammer, Submitted with Debtor's Petition 283

Chandler Act. I ask that such additional trustee, to be appointed, be Samuel Silverman, Esq., of 50 Broad Street, New York City.

Said Samuel Silverman, Esq. has been and still is the vice-president and general counsel of the debtor, is familiar with its affairs, and has had considerable experience in the actual management of real estate. He is an attorney-at-law, duly admitted to practice before this Court, has enjoyed and still enjoys a reputable standing before both the Bench and the Bar. I am certain that he will fulfill each and every qualification imposed by law upon trustees to be appointed in such proceedings. 284

(c) The names of all the officers and directors of the debtor, and their present salaries are as follows:

Name	*Office Held*	*Salary*
Gussie Hammer	President	None
Samuel Silverman	Vice-President	None
Abraham J. Hammer	Treasurer	None
Gussie Hammer	Secretary	None

GUSSIE HAMMER

285

Sworn to before me this
15th day of September, 1941.

MIRIAM HARMALEN
Notary Public, Bronx County
N. Y. Co. Clk's No. 167, Reg. No. 185-H-42
Kings Co. Clk's No. 241, Reg. No. 2321
Commission Expires March 30, 1942

286 **Order Dated September 17, 1941, Approving Petition**

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE]

This cause coming on to be heard at this time on the
287 petition of Marine Harbor Properties, Inc., hereinafter called the debtor, verified the 15th day of September, 1941, and the affidavit of Gussie Hammer, Secretary of the debtor, sworn to the 15th day of September, 1941, and the Court having heard the arguments of counsel and being fully advised in the premises,

Upon motion of Friedland & Friedland, Esqs., attorneys for the debtor, it is

FOUND, ORDERED, ADJUDGED AND DECREED:

(1) That the Court is satisfied that the said petition complied with Chapter X of an act entitled "An Act to
288 Establish a Uniform System of Bankruptcy Throughout the United States," approved June 22, 1938, and acts amendatory thereof, hereinafter referred to as the Bankruptcy Act, and that such petition has been filed in good faith.

(2) That said petition be, and it hereby is approved as properly filed under Chapter X of the Bankruptcy Act.

(3) That the debtor is unable to meet its debts as they mature.

(4) That by reason of the facts set forth in said petition, relief under Chapter X is required, and that there is

no adequate remedy save through the granting of such relief.

(5) That Maurice Rubinger, Esq., attorney at law, 160 Broadway, N. Y. C., be, and he hereby is appointed trustee to take possession of the assets of this estate and to continue to act as such trustee until further order of this Court.

(6) That Samuel Silverman, be, and he hereby is appointed additional trustee, pursuant to and in accordance with Section 156 of the Bankruptcy Act.

(7) That Maurice Rubinger and Samuel Silverman, the 290
trustees hereinabove appointed, shall have all of the title to the assets of the debtor, and shall exercise, consistently with the provisions of Chapter X, all of the powers of a trustee appointed pursuant to such chapter, subject, nevertheless, at all times, to the control of this Court and to such limitations, restrictions, terms and conditions as this Court may, from time to time, impose and prescribe, and, without limiting the generality of the foregoing, shall be and hereby are:

(a) authorized to continue in business of all and singular its business, assets, and properties, real, personal and mixed, and of every name and nature, 291
wheresoever situated, and to preserve, manage, operate and use the same, and to carry on its business as an entirety, and to exercise all and singular its rights, authorities, franchises, and privileges, for such manner and to such extent as to it may seem necessary or desirable.

(b) authorized to prosecute, become a party to, intervene in, compromise and defend suits and actions at law, or in equity or otherwise in which it may have any interest as plaintiff, defendant, or otherwise.

292 *Order Dated September 17, 1941, Approving Petition*

(c) authorized to continue the operation of its business as an entirety in usual course and to that end, in its discretion, to employ and discharge, and, subject to the provisions of paragraph "9" (b) hereof, to pay compensation, salaries and wages of such managers, superintendents, bookkeepers, agents and employees, as it may deem necessary or advisable in connection with the custody and control, preservation and operation and management of its estate, or necessary and desirable to avoid detriment thereto; to perform its existing contracts, including leases, to
293 the extent that performance thereof may seem desirable to it; to purchase any merchandise or other personal property required in the regular and usual conduct of its business, and to enter into, perform other contracts in the regular course and conduct of its business, to let and sub-let all or part of the property owned by it, to incur or discharge any and all expenses which it may deem necessary or advisable for any of said purposes or to the end that this business may be continued, operated and managed as an entirety, according to the customary and usual manner of conducting similar businesses, until the further order of
294 this court, in the premises; provided, however, that nothing herein contained shall be deemed affirmance or disaffirmance of any contract or lease of the debtor; that in such affirmance or disaffirmance shall be by virtue of a written notice of an election to affirm or disaffirm by said debtor approved by this court, and not otherwise.

(8) That Mortimer Rubenstein, as receiver of the debtor's property, appointed by the Supreme Court of the State of New York, County of Kings, be, and he hereby is authorized, permitted and directed to surrender, transfer, turn over and

assign all of the assets of the debtor's estate unto the trustees herein, within five days after said nominated trustees shall have duly qualified as such, and a certified copy of this order served upon said Mortimer Rubenstein; and he is further authorized, directed and permitted to account to the said trustees, for all of his acts, conduct and affairs during his term as receiver of the debtor's estate in the Supreme Court of the State of New York, County of Kings, as of the date of such surrender.

(9) That the trustees herein, upon qualification, shall open new books of account as of the opening of business 296
immediately upon qualification and the accounting to them by Mortimer Rubenstein, as receiver, and they shall cause to be kept due and proper accounts of earnings, expense, receipts and disbursements, of the debtor estate hereunder, and the trustees shall preserve proper vouchers for all payments made on account thereof, and shall deposit the monies coming into their hands, in any such banks designated by this Court as depositories of funds of debtor's estate, as shall be selected by such trustees, or in any other bank or banks as may be hereinafter approved by this Court.

(10) That without the further order of this Court, said trustees shall not pledge or create any lien on any of the 297
profits or assets of the debtor, nor shall they pay any salary or other compensation to any of its officers, except as herein provided.

(11) That the said trustees be, and they hereby are authorized in their discretion, from time to time, until further order of this Court, to pay and discharge, out of any funds in or herein coming into their hands, and available for such purposes in the following order:

(a) All expenses and charges incurred in the operation of the business hereby authorized in preserving and maintaining the estate of the debtor.

298 *Order Dated September 17, 1941, Approving Petition*

(b) All claims for accrued wages of employees for services rendered prior to the date of this order but remaining unpaid at the date hereof and entitled to priority in payment under the provisions of the Bankruptcy Act, to the end that the operation of the business of the debtor may not be interfered with or interrupted.

(c) All taxes and charges of the nature thereof lawfully incurred or to be incurred in the operation of the business or imposed upon said property so far
299 as it may deem such payments necessary or advisable in connection with the preservation of its property, and the operation of its business.

(12) That all persons, firms, or corporations, including sheriffs, marshals, or other officers, agents or attorneys, representatives, or employees, whether creditors or claiming to be creditors, or having or claiming to have any right, title or interest in and to the property of the debtor, are hereby enjoined and restrained from interfering with, transferring, selling or disposing of any of the property or income constituting the debtor's estate, and all creditors of the debtor and all other persons, firms, or corporations, are hereby enjoined
300 from commencing or continuing any suit or suits against the debtor until after final decree in these proceedings, and from levying any attachments, executions, or other processes upon or against any of the properties constituting the debtor's estate, or from taking or attempting to take into their possession any part of the property constituting the debtor's estate, and from doing any act whatsoever to interfere with the possession, operation, or management by the trustees of the properties and business constituting its estate, or from interfering in any way with the trustees in the discharge of their duties or interfering in any way in the administration

or disposition of the affairs and property constituting the debtor's estate.

(13) That the proceedings shall be and are hereby referred to P. B. Olney a referee in bankruptcy, as referee, to hear and determine any and all matters not reserved to the Judge by the provisions of Chapter X of the Bankruptcy Act, and Special Master, to hear and report generally upon all matters reserved to the Court by the provisions of Chapter X of the Bankruptcy Act.

(14) That within 15 days after the trustees herein shall 302
have qualified as such, they are hereby authorized, and directed to prepare and file herein a list of the creditors of each class, showing the amounts and character of their claims and securities, and so far as known, the name and the postoffice address or place of business of each creditor; and a further list of the debtors, stockholders, of each class, showing the number and kind of shares registered in the name of each stockholder, and the last known post-office address or place of business of each stockholder.

Sept. 17, 1941.

JOHN BRIGHT
U. S. D. J.

303

Trustees Bond in proper form and to be approved by the undersigned or a judge of this court, fixed at $10,000.

JOHN BRIGHT
U. S. D. J.

304

Stipulation as to Exhibits

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

IN THE MATTER

of

305 MARINE HARBOR PROPERTIES, INC.,
Debtor.

IT IS HEREBY STIPULATED AND AGREED that the following exhibits annexed to the petition of The Mortgage Corporation of New York as Trustee may be eliminated from the printed transcript of record on appeal:

Exhibit B—Notice of proceeding, proposed plan, etc.

306 Exhibit C—Interlocutory order dated July 11, 1938.

Exhibit F—Interlocutory order dated November 17, 1934.

Exhibit G-1—Extension agreement dated March 11, 1935.

Exhibits H and I—Notice of pendency, summons and complaint in foreclosure action.

Stipulation as to Exhibits 307

Exhibit J—Order appointing receiver in New York State Supreme Court, dated May 3, 1941.

Dated, New York, October 14, 1941.

FRIEDLAND & FRIEDLAND,
Attorneys for Debtor-Appellee.

HUGHES, HUBBARD & EWING,
Attorneys for Manufacturers Trust Company, formerly The Mortgage Corporation of New York, as 308
Trustee, Petitioner-Appellant.

MAURICE RUBINGER,
Trustee-Appellee.

SAMUEL SILVERMAN,
Trustee-Appellee.

GEORGE ROSLING,
Attorney for Mortimer Rubenstein, as Receiver-Appellee.

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310

Stipulation as to Record

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE]

IT IS HEREBY STIPULATED AND AGREED that the foregoing is a true and correct transcript of the record of the said District Court, in the above-entitled action, as agreed upon by the
311 parties hereto.

Dated New York, October 14, 1941.

FRIEDLAND & FRIEDLAND,
Attorneys for Debtor-Appellee.

HUGHES, HUBBARD & EWING,
Attorneys for Manufacturers Trust Company, formerly The Mortgage Corporation of New York, as Trustee, Petitioner-Appellant.

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MAURICE RUBINGER,
Trustee-Appellee.

SAMUEL SILVERMAN,
Trustee-Appellee.

GEORGE ROSLING,
Attorney for Mortimer Rubenstein, as Receiver-Appellee.

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Clerk's Certificate

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

[SAME TITLE]

I, GEORGE J. H. FOLLMER, Clerk of the District Court of the United States of America, for the Southern District of New York, do hereby certify that the foregoing is a correct transcript of the record of the said District Court in the above-entitled proceeding, as agreed upon by the parties.

314

IN WITNESS WHEREOF, I have caused the seal of the said court to be hereunto affixed at the City of New York, in the Southern District of New York, this day of October, in the year of our Lord One thousand, nine hundred, forty-one and of the independence of the said United States, the One hundred sixty-sixth.

GEORGE J. H. FOLLMER,
Clerk.

315

[fol. 106] UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT, OCTOBER TERM, 1941

No. 107

(Argued October 20, 1941. Decided January 10, 1942)

In the Matter of MARINE HARBOR PROPERTIES, INC., Debtor-Appellee,

MANUFACTURERS TRUST COMPANY (successor by merger to The Mortgage Corporation of New York), as Trustee for the benefit of certificate holders in mortgage guaranteed by Bond and Mortgage Guarantee Company, Guarantee No. 181,568, Petitioner-Appellant,

MAURICE RUBINGER, Trustee of Marine Harbor Properties, Inc., SAMUEL SILVERMAN, additional Trustee of Marine Harbor Properties, Inc., and MORTIMER RUBENSTEIN, Foreclosure Receiver, Appellees

Appeal from the District Court of the United States for the Southern District of New York

Proceeding by Marine Harbor Properties, Inc., for reorganization under Chapter X of the Bankruptcy Act, 11 [fol. 107] U. S. C. A. § 501 *et seq.* Manufacturers Trust Company as trustee for holders of participation certificates in a first mortgage upon the debtor's real estate appeals from an order denying its application to dismiss the debtor's petition and to vacate a prior *ex parte* order approving the same. Reversed.

Before Swan, Chase and Frank, Circuit Judges

Hughes, Hubbard & Ewing, Attorneys for Appellant; Curtiss E. Frank and Orville H. Schell, Jr., of Counsel.
Friedland & Friedland, Attorneys for Debtor-Appellee.
George Rosling, Attorney for Mortimer Rubenstein, Receiver-Appellee.
Chester T. Lane, General Counsel, and J. Anthony Panuch, Attorney, for Securities and Exchange Commission; George Zolotar and Mortimer Weinbach, of Counsel.

SWAN, *Circuit Judge:*

On September 17, 1941 the debtor obtained an *ex parte* order approving as properly filed under Chapter X of the Bankruptcy Act its petition for reorganization. The Mortgage Corporation of New York, as trustee for mortgage certificate holders, forthwith applied to the district court to vacate its order of approval and to dismiss the debtor's [fol. 108] petition as lacking the good faith required by section 141, 11 U. S. C. A. § 541. After a hearing upon supporting and opposing affidavits, the court denied the application. This order is before us on appeal by Manufacturers Trust Company, the successor by merger of The Mortgage Corporation of New York. The Securities and Exchange Commission filed its appearance in the district court pursuant to section 208, 11 U. S. C. A. § 608, and has presented in this court a brief and argument in support of the order.

So far as relevant to the present controversy section 146 of the Act, 11 U. S. C. A. § 546, provides that

"Without limiting the generality of the meaning of the term 'good faith', a petition shall be deemed not to be filed in good faith if—

* * * * * * *

(3) it is unreasonable to expect that a plan of reorganization can be effected; or

(4) a prior proceeding is pending in any court and it appears that the interests of creditors and stockholders would be best subserved in said prior proceeding."

Each of these clauses, the appellant contends, requires dismissal of the debtor's petition.

The debtor's sole asset is an apartment building in Brooklyn of the value, including the land, of not more than $350,000. The premises are subject to a first mortgage in the principal amount of $370,000, with arrears of interest and taxes which bring the indebtedness secured thereby to approximately $400,000 as of October 1, 1941. There is also a second mortgage for $25,000, a third and fourth mortgage for $2,000 each, a balance of $3,000 due on equipment purchased on conditional bills of sale, and unsecured indebted- [fol. 109] ness in an amount not specified. The first mortgage was made in 1931 by a predecessor in title of the debtor to Title Guarantee & Trust Company, which issued and sold to

the public participation certificates therein guaranteed by Bond & Mortgage Guarantee Company, hereafter called the guarantor. In August 1933 the guarantor was taken over by the Superintendent of Insurance of the State of New York for rehabilitation under the Schackno Act, N. Y. Laws 1933, Ch. 745. In this proceeding a plan of reorganization of the rights of certificate holders in the said first mortgage was approved by the Supreme Court of Kings County on December 6, 1934, with the approval of two-thirds of the certificate holders and with the consent of the debtor. Under this plan the mortgage was extended to December 1, 1937 and interest was reduced from 6% to 5%. Subsequently, by order of December 6, 1938 the state court modified the plan to the extent of appointing The Mortgage Corporation of New York as trustee of the bond and mortgage under an approved form of declaration of trust. This order provided that the court should retain jurisdiction until complete liquidation of the trust estate, and that "the trustee, or any other interested party herein" might apply for other and further relief. After the mortgage matured on December 1, 1937 the debtor continued to pay interest and taxes until April 1, 1941. On that date it defaulted, although the earnings of the property were sufficient to cover interest and taxes. Shortly thereafter foreclosure proceedings were begun and the receiver appointed therein has been in continuous possession of the mortgaged premises since May 6, 1941. The appellant and its predecessor trustee have conducted negotiations with the debtor with regard to a further extension and modification of the mortgage but no agreement was reached and no proposed modification was presented to the certificate holders or to the state court. On [fol. 110] September 17, 1941 the debtor filed in the district court its petition for reorganization under Chapter X of the Bankruptcy Act.

Since the amount owing under the first mortgage is largely in excess of the value of the premises, it is apparent that no equity remains for junior lienors, unsecured creditors or stockholders of the debtor. The appellant, therefore, argues that it is unreasonable to expect that a plan of reorganization can be effected, and that section 146(3) of the Act, 11 U. S. C. A. § 546(3) requires dismissal of the debtor's petition. But as the Supreme Court stated in *Case* v. *Los Angeles Lumber Co.*, 308 U. S. 106, 131, approval of a debtor's petition is no indication that its stockholders will participate in the plan. Nor is the fact of insolvency sufficient to prove

that the petition was filed in bad faith. *In re Castle Beach Apartments*, 113 F. 2d 762 (C. C. A. 2); *In re Central Funding Corp.*, 75 F. 2d 256, 261 (C. C. A. 2); *In re Julius Rochrs Co.*, 115 F. 2d 723, 724 (C. C. A. 3). And this is further demonstrated by section 179, 11 U. S. C. A. § 579, where the implication is clear that a plan may be effected, even though the debtor has been found to be insolvent. It is true that when the first mortgage security is inadequate and the debtor has no assets other than the mortgaged premises, it is difficult to conceive of a plan, which the court could approve as fair and equitable, that would give anything to lienors or creditors other than the first mortgage certificate holders, unless new money is put in. But even if it be unreasonable to expect that new money will be forthcoming or that any plan can be effected which will provide anything for the debtor or its shareholders, we do not think clause 3 of section 146, 11 U. S. C. A. § 546(3) requires dismissal of the debtor's petition; the reorganization may still go on in the interest of such creditors as shall be found entitled to share in the debtor's assets. No plan was, or could be, submitted by the debtor with its petition, and we see no error in the district [fol. 111] judge's conclusion that the trustees in reorganization should have an opportunity to explore the possibilities and propose a plan before he should decide that it was unreasonable to expect that any reorganization could be effected. Cf. *In re Blinrig Realty Corp.*, 114 F. 2d 100 (C. C. A. 2).

The second branch of the appellant's argument presents the contention that the pending state court reorganization proceedings require dismissal of the debtor's petition pursuant to section 146(4), 11 U. S. C. A. § 546(4). Primary reliance is placed on the recent decision of this court in *Brooklyn Trust Co.* v. *Rembaugh*, 116 F. 2d 838. In the *Rembaugh* case a finding of good faith was reversed on facts closely parallel to those of the case at bar. There are, however, slight differences which the debtor seizes upon as a ground for distinction. In *Rembaugh*, the plan of reorganization, as promulgated in the state court, provided in the same order for appointment of a trustee and for extension of the mortgage, and the mortgage had not matured when the debtor defaulted and foreclosure was commenced. Therefore, it is urged, the state proceeding was still pending when the debtor's petition was filed, while that is not the situation in the case at bar. With the latter conclusion we cannot agree. It is true that the original plan of re-

organization provided only for an extension of the mortgage to December 1, 1937, but the 1938 proceeding in which a trustee was appointed was denominated a "modification" of the original plan and the court expressly reserved jurisdiction to grant other relief on the application of any "interested party." The debtor had consented in open court to the original plan, had not objected to the modification, and had made payments to the trustee in conformity with it for more than two years. We think the debtor had assented to the modified plan as fully as had the debtor in the *Rembaugh* case. The two cases cannot be distinguished [fol. 112] on this ground. The district court attempted to distinguish them on the ground that "here the debtor has endeavored on two occasions to present modified plans for relief, but on each occasion has been rebuffed by the trustee" and given no opportunity to communicate with the certificate holders. But the debtor made no attempt to bring its proposals to the attention of the state court in the pending proceeding, as we think it was entitled to do as an "interested party"; had it done so its proposals, with the court's approval, could have been presented to the certificate holders. That proceeding provides adequate means to reorganize the mortgage and protect the rights of all certificate holders whose interests alone exhaust the debtor's property. In the *Rembaugh* case we held the element of good faith to be lacking because a debtor, which had voluntarily submitted to a plan for reorganization in the state court but found compliance therewith irksome, invoked federal jurisdiction instead of seeking relief in the state court. Although the debtor did not itself propose a plan, it assented to one proposed by another and was, we said, "in the position of one who voluntarily submitted the plan for the reorganization in the state court"; and the opinion enunciated the following rule: "After electing to have the mortgage provisions modified in the state court proceedings it could not escape from the consequences of the plan to which it had assented by simply filing a petition for reorganization in the federal court while the proceedings in the state court were still pending." Unless we are to overrule the *Rembaugh* case, we think the same decision must be made here.

A majority of the court is of the opinion that the *Rembaugh* case should be given effect here to prevent a debtor, who has assented to a plan which is being supervised by the state court in reorganization proceedings still pending there,

from flouting that jurisdiction by filing a petition in the dis-
[fol. 113] trict court. The applicable principle, as was said in the *Rembaugh* case, is not an absence of good faith in the filing of the new petition in the broad meaning of those words but a special instance of a lack of good faith flowing from the personal disqualification of the debtor. Section 146 (11 U. S. C. A. § 546) expressly disclaims any limitation upon the generality of the meaning of good faith and subsection 4 of that section is but one special instance of what will show a disabling absence of it on the part of a debtor and is not to be confused with what controls here. Nor is it relevant that others than the debtor may have the right to file a petition in the district court regardless of the pendency of a petition in some other court or what the debtor has done there. Until such a petition has been filed, the jurisdiction of the court has been invoked only by the debtor's petition and properly invoked only if the petition has been filed in good faith. Section 141 (11 U. S. C. A. § 541).

Accordingly, the order is reversed.

FRANK, *C. J.*, dissenting:

My colleagues base their decision, requiring dismissal of the petition, on Section 146(4), as they consider it to have been interpreted in the earlier decision of this court in *Brooklyn Trust Co.* v. *Rembaugh*, 110 F. (2d) 838. That decision has been severely criticized. See 18 N. Y. U. L. Q. Rev. (1941) 399, 418; cf. 412-443.

I am wholly in accord with the general policy of adherence to rulings in earlier decisions. But there are well-recognized exceptions to that policy, and I think that the instant case comes squarely within those exceptions. Undeniably, in order to achieve impartial administration of justice, "equality before the law," and legal certainty, as far
[fol. 114] as is practicable,[1] it is important, generally, that a

[1] As to how far it is practicably to procure such certainty through *stare decisis*, see, e.g., Wigmore, *The Judicial Function*, in *The Science of Legal Method*, xxxvi-xxxix; Wigmore, *Problems of Law*, 79-80; Dillon, *The Laws and Jurisprudence of England and America*, 242 ff; Dickinson, *Administrative Justice and The Supremacy of Law*, 210, 231-232; Kessler, *Theoretic Bases of Law*, 9 Un. of Chic. L. Rev. (1941) 98, 107; Green, *Judge and Jury*, 79-80.

court should not deviate, except prospectively,[2] from its own decision in a prior case, even if that decision was in error, especially where such deviation will harm persons who acted in reliance upon that decision—as, for instance, a decision assigning specific legal consequences to specific words in a deed or lease. But that policy loses its force when there has been no such reliance; the question relates solely to procedure; it is plain, on reconsideration in a subsequent case, that the decision in the prior case involved an interpretation of a statute which defeats an important purpose of the legislature, and such interpretation arose from a failure of the court in the prior case to consider matters not called to its attention by the parties.

In *Webster* v. *Fall*, 277 U. S. 507, 511, the court said: "Counsel for appellant directs our attention to other cases, where this court proceeded to determine the merits notwithstanding the suits were brought against inferior or subordinate officials without joining the superior. We do not stop to inquire whether all or any of them can be differentiated from the case now under consideration, since *in none of them was the point here at issue suggested or decided. The most that can be said is that the point was in the cases if anyone had seen fit to raise it. Questions which* [fol. 115] *merely lurk in the record, neither brought to the attention of the court nor ruled upon, are not to be considered as having been so decided as to constitute precedents.* See *New* v. *Oklahoma*, 195 U. S. 252, 256; *Tefft, Weller & Co.* v. *Munsuri*, 222 U. S. 114, 119; *U. S.* v. *More*, 3 Cr. 159, 172; *The Edward*, 1 Wheat. 261, 275-276." Cf. *Massachusetts* v. *Mellon*, 262 U. S. 447, 486. In *Erie R. Co.* v. *Tompkins*, 304 U. S. 64, the Supreme Court in 1938 over-ruled a statutory interpretation which it had frequently applied over a period of ninety-six years.[3]

[2] As to prospective over-ruling of precedents, see *Great Northern Ry. Co.* v. *Sunburst Oil & Refining Co.*, 287 U. S. 358, 365-366; *People* v. *Maughs*, 149 Cal. 253, 86 Pac. 187; *People* v. *Ryan*, 152 Cal. 364, 92 Pac. 853; cf. Cardozo, *The Nature of the Judicial Process*, 146-149; Wigmore, loc. cit.

[3] See *Burnet* v. *Coronada Oil & Gas Co.*, 285 U. S. 393, 406, note 1, for a list of cases in which the Supreme Court had previously over-ruled its prior decisions. There have been other such cases, since *Erie* v. *Tompkins;* among them are *Nye* v. *United States*, 313 U. S. 33 (1941); *California* v. *Thompson*, 313 U. S. 109, 116 (1941); *Olsen* v. *Nebraska*, 313 U. S. 237 (1941).

In the *Rembaugh* case, briefs were filed by the debtor and by the trustee, appointed in the state court proceeding. No certificate-holder appeared.[4] Indeed, the state court trustee asserted in its brief in that case that it alone could be heard to speak for the certificate-holders.[5] Without at all suggesting any lack of integrity on the part of that state court trustee, it is appropriate to observe that it had a selfish interest, not identical with the interests of the certificate-holders, in having the state court proceeding continue, because the trustee derived emoluments therefrom which would terminate if the Chapter X proceeding was not dismissed.[6] As a result, important considerations affecting [fol. 116] the interests of the certificate-holders were not pressed, and the case was argued as if the major factors were the prior conduct of the debtor (regarded as giving rise to some kind of an estoppel), and the protection of the debtor's interests. Consequently, this court, on the basis of such limited argument, said nothing whatever in its opinion in the *Rembaugh* case as to the purpose and effect of those provisions of Section 146(4) which explicitly refer to the protection of the interests of creditors. Those provisions have, in the instant case, been called to our attention by the S. E. C., which is a party here, as it was not in the *Rembaugh* case. And, as no one who acted in reliance on the decision in that case will be harmed by our failure here to regard it as a binding precedent, we should disregard it, since, if we do not do so, we will, as I shall try to show, be frustrating important objectives of Congress in enacting Chapter X.

Here no "rule of property" is involved. Peculiarly in such a case as this, it is appropriate to bear in mind that "*stare decisis* in statutory contruction, is a useful rule, not an inexorable command,"[7] and that, although it is a doctrine

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[4] As the Chapter X proceeding never went beyond the filing of the petition, presumably no notice was given to certificate-holders.

[5] The trustee went so far as to maintain in its brief that if the Chapter X proceeding continued, it alone, and no certificate-holder, could vote on a plan proposed therein.

[6] A brief, *amicus curiae*, was filed by trustees appointed in other state court proceedings. Of course, they too had such an interest in the continuance of their emoluments.

[7] *Erie R. Co.* v. *Tompkins*, 304 U. S. 64, 92.

"tending to consistency and uniformity of decision," it "is not inflexible."[8] It has been well said that, although "inconsistent decisions rendered in disregard of the principle of *stare decisis* tend to make the law uncertain and unstable," and a court "may hesitate to disregard a precedent," nevertheless "it is free to do so when convinced that its earlier determination is unsound."[9] "Mere precedent alone is not sufficient to settle and establish forever a legal principle. Infallibility is to be conceded to no human tribunal."[10] While [fol. 117] uniformity is important, "we must not allow a Blackstonian optimism to blind us to remediable defects * * *. Above all, we must not assign to precedent a sacramental magic in opposition to the principles of logic and justice."[11] It is not the duty of courts, in all circumstances, to perpetuate their errors.

The majority opinion recognizes that it is not at all necessary in order to avoid dismissal of a petition pursuant to Section 146(3), to show that "it is reasonable to expect that a plan of reorganization be effected," in which the debtor or its stockholders will participate. In the instant case, for instance, where, as the majority opinion states, the claims of the certificate-holders exhaust the debtor's property and there is no equity for the stockholders, there is no reason why (unless the stockholders furnish needed new money or other needed new consideration) a plan cannot be effected by which, without the expense or delay involved in foreclosure, the property will promptly be turned over to a new company, having no debts, all of the stock being ratably distributed among the certificate-holders. That some such plan[12] can reasonably be expected to be effected under Chapter X is, we all agree, sufficient to prevent a dismissal pursuant to Clause (3).

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[8] *Hertz* v. *Woodman*, 218 U. S. 205, 212.

[9] *Sears, Roebuck & Co.*, v. *9 Ave.-31 St. Corp.*, 274 N. Y. 388, 400.

[10] *Leavitt* v. *Morrow*, 6 Oh. St. 71, 78.

[11] Allen, *Law in the Making* (1927) 188.

[12] On the all-common-stock plan, see *Matter of Flour Mills of America, Inc.*, 7 S. E. C. 1, 27. In the instant case, such a plan might, in the alternative, provide for a relatively small amount of new debt, and all the debt obligations and stock might be distributed among the certificate-holders.

But the majority opinion, in directing a dismissal under Clause (4), follows the *Rembaugh* case in holding that the controlling factor is the earlier conduct of the debtor in the pending state court proceedings. Such an interpretation of Clause (4) disregards its plain language. By its express [fol. 118] terms, Clause (4) calls for a dismissal of a petition when "a prior proceeding is pending in any court and it appears that the *interests of creditors* and stockholders would be best subserved in said prior proceeding." Clearly, it should be alone sufficient, to prevent dismissal, under (4), that "*the interests of creditors*" will not be best subserved in the prior proceeding. And particularly is that true when, as here, the claims of the creditors exceed the value of the assets, so that there is small likelihood that the stockholders will have any interests.

But in the *Rembaugh* case, the court acted as if Clause (4) provided for dismissal "if it appears that the interests of the stockholders alone will be as well subserved in the prior proceedings; if that appears, then no consideration shall be given to the question whether the interests of the creditors will be best subserved in such proceeding." The majority opinion here, in effect, accepts that interpretation. It says that "*the debtor had assented* to the modified plan as fully as had the debtor in the *Rembaugh* case"; and that "*the debtor made no attempt to bring its proposal to the attention of the state court*"; that "in the *Rembaugh* case we held the element of good faith to be lacking because a *debtor*, which had voluntarily submitted to a plan for reorganization in the state court, but found a compliance therewith irksome, invoked federal jurisdiction instead of *seeking relief in the state court.*"

But why should such conduct of the debtor preclude careful scrutiny by the federal court of what is best for creditors, especially in this case where the majority finds that the interests of the creditors "alone exhaust the debtor's property"? Why, in such a case, should attention be confined solely to the conduct of the debtor and the interests of its stockholders? In any sort of case, the interests of creditors should be given precedence over those of stock- [fol. 119] holders. But in a case like this, it is especially strange to ignore the best interests of the creditors (the certificate-holders) and to order dismissal under Clause (4), either because of some sort of estoppel of the debtor

or because its interest (not that of the creditors) can be as well subserved in the prior proceeding.

The *Rembaugh* interpretation of Clause (4), adopted by the majority here, in effect reads out of the statute the words "the interests of the creditors." And in doing so, it defeats a major purpose of Congress in substituting Chapter X for former Section 77-B. Here we reach the basic error in the *Rembaugh* decision:

The elaborate studies of the S. E. C., and of the congressional committees, which led to the enactment of Chapter X demonstrated that plans had theretofore frequently been adopted in state court proceedings, and even under Section 77-B, which were not "fair and equitable" or which, although "fair and equitable," were not "feasible." For present purposes, it will suffice to consider the way in which the criterion of "feasibility" is applied under Chapter X.

A plan may limit participation to those equitably entitled to participation and provide for distribution of the new securities according to the priorities of such participants in the old enterprise; it is, then, "fair and equitable." But study disclosed that, under many such a plan, there was set up a new enterprise with such an excessive amount of new debt obligations that new defaults soon occurred, compelling a new reorganization in a short time.[13] Such a plan is not [fol. 120] "feasible." Because Congress found that plans lacking feasibility had frequently been adopted but were undesirable, it expressly ruled them out. And one of the principal purposes of Chapter X, in providing for advisory reports by the S. E. C., was to see to it that the district court will be properly informed, before approving a plan

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[13] There are other factors which may render a plan not "feasible." For instance, a plan may call for the issuance of preferred stock with cumulative dividends which cannot be expected to be earned. On feasibility generally (see Note (1941), 18 New York Un. Law Q. Rev. 399, 466. Among the standards applied is the requirement of a capital structure consistent with expected future income [*Matter of San Francisco Bay Toll-Bridge Co.*, 6 S. E. C. 863, 867 (1940); cf. 51 Yale Law J. 86, 91, 96] and of a workable capital structure (S. E. C. Report on Protective and Reorganization Committees, Part VIII, 159-161).

for submission to the old security-holders, as to whether the plan is "feasible." Experience under Chapter X has shown that the district courts, on the basis of such S. E. C. advisory reports, have rejected many plans, or caused them to be modified, because of lack of "feasibility."

Consequently, before dismissing a petition under Section 146(4) because a prior proceeding is pending, the district court, in deciding whether "the interests of the creditors would be best subserved in said prior proceedings," must consider, among other things, whether, in the pending state court proceedings, there are safeguards, at least equivalent to those afforded by Chapter X, to ensure that a plan adopted in the state court proceeding will be not only "fair and equitable" but also "feasible." If the district court finds, for instance, that the value of the property is so small that creditors alone can participate, and that there is only one class of creditors entitled to participation, it must then, before dismissing a petition under Section 146(4), ask and answer this question: Are there safeguards, at least as good as those under Chapter X, to ensure that a plan adopted in the state court—even if it is sure to allocate all the new securities to those creditors—will be so devised as to meet the test of feasibility? It must consider, for instance, whether there are methods, sure to operate in the state court, and as adequate as those under Chapter X, for ascertaining whether it is feasible to issue any new debt-obligations, and, if so, what is feasible as to the principal amount of such obligations and as to the rate of interest.

[fol. 121] It may perhaps be said that such an interpretation of Section 146(4) means that no petition will ever be dismissed thereunder, i.e., that such an interpretation renders Clause (4) functionless. But that is not true. A case can easily arise where, before the Chapter X petition was filed, a plan had been proposed in the pending state court proceedings, and where the district court [14] finds that that state court plan is both "fair and equitable," and "feasible," and that the parties will be protected by safe-

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[14] It would seem appropriate that it obtain an advisory report from the S. E. C. as an aid to making its determination.

guards substantially equivalent to those of Chapter X.[15] In such a case, the petition should be dismissed under Clause (4). If, in the instant case, some such plan had been proposed in the state court before the petition was filed, and the district court could thus have satisfied itself as to the protection of the interests of the certificate-holders, and had done so, then a dismissal would be proper under Clause (4).[16]

But that is not this case. Here the "plan" approved by the state court in December, 1934, as modified in December, [fol. 122] 1938, merely provided for an extension of the mortgage and retention of jurisdiction by the state court until complete liquidation. The debtor subsequently defaulted in payment of interest on April 1, 1941; foreclosure proceedings have been begun in the state court; a state court receiver is in possession; and unsuccessful negotiations for further extension and modification of the mortgage have been conducted. *If, then, there is not to be liquidation, a new plan must be adopted. And no such new plan had been brought forward in the pending state court proceedings, before the petition was filed under Chapter X, nor do we know of any which has, since then, been proposed.*

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[15] One of the important new safeguards of Chapter X is that, in certain kinds of cases, (1) the court must receive an S. E. C. advisory report and must thereafter find the plan fair and equitable and feasible *before* the plan is submitted to those interested in the estate, and (2) those voting on the plan must, *before voting*, have in their hands that advisory report. It may well be, therefore, that, in the supposititious case discussed in the text, not only should the district court, before its dismissal of the petition, find the state court plan fair and equitable and feasible, but should condition its dismissal on the distribution to the creditors, before they vote on the plan of the S. E. C. advisory report. On the public interest in stable investments, see *Matter of San Francisco Toll-Bridge Co.*, 6 S. E. C. 863, 867, 872. On the importance of the judgment of an expert impartial agency as to the issue of valuation, see 51 Yale Law J. 85, 93.

[16] No doubt there might be other situations in which the court might appropriately find that the interests of creditors and stockholders would be best subserved by continuation of the state proceeding.

My colleagues say, and I agree, that the district judge correctly concluded that, so far as Clause (3) is concerned, trustees in reorganization under Chapter X "should have an opportunity to explore the possibilities and propose a plan before he should decide that it was unreasonable to expect that any reorganization could be effected." But my colleagues, out of deference to the *Rembaugh* decision, have decided that, nevertheless, there must be a dismissal under Section 146(4) solely because of the debtor's conduct in the prior and pending proceeding.

True, in so deciding, they say that that prior proceeding "provides adequate means to reorganize the mortgage and protect the rights of all certificate-holders whose interests alone exhaust the debtor's property." But that single reference in their opinion to the protection of the interests of certificate-holders, they support by nothing whatever; there is no demonstration that those interests will be "best subserved" in that ~~proceeding~~, i.e., that there will be safeguards for their interests equivalent to those provided by Chapter X.

Appellant argues that such protection will be afforded in the state court proceedings, and they point particularly to [fol. 123] the function of the Bureau of Trust Supervision in advising the state court as to the fairness of proposed plans. But proof that protection will be provided requires far more than a mere reference to the statute establishing this agency. Absent a more convincing showing, it is impossible for me to concur in a decision dismissing the petition under Section 146(4).

There remains to be considered the suggestion of my colleagues that, quite apart from Clause (4), the conduct of the debtor in the state court demonstrates that the petition was not "filed in good faith," and that such considerations must be regarded because Section 146 begins with the words "Without limiting the generality of the meaning of the term 'good faith' * * *." To such a suggestion, there are, I think, these answers:

My colleagues rest their decision here on the *Rembaugh* case. But in that case this court rejected the argument which my colleagues now advance, saying that there was no "substantial ground for attacking the exercise by the trial judge of discretion to approve the petition as one filed in good faith within the broad meaning of that term." More important is the fact that Congress in Clause (4) explicitly

covered the subject of what effect should be given to "a prior proceeding * * * pending in any court." It said that when there was such a proceeding, then "good faith" was to be tested by the criterion, already discussed, whether the interests of creditors and stockholders would be best subserved therein. To set up other tests of "good faith," concerning such prior proceedings, is, therefore, to enlarge on a subject with which Congress exhaustively dealt in Clause (4). Nothing in the legislative history of the statute justifies such a departure from its language. And the courts should hesitate thus to depart from that language when, as here, to do so means that, realistically considered, the best [fol. 124] interests of creditors—which Congress clearly regarded as of major importance in determining whether a prior proceeding should be the basis of dismissal—will be injured. Anyone familiar with the realities of corporate reorganizations—as Congress was when it enacted Chapter X after the elaborate studies of that subject by the S. E. C. and the Congressional Committees—knows that scattered individual security-holders, such as the individual certificate-holders in this case, are not at all informed as to their rights. It is true that, under Section 126, three such certificate-holders, having claims aggregating at least $5,000, can file a petition for reorganization under Chapter X, notwithstanding the pendency of state court proceedings. But, ignorant of their theoretical rights, as most such security-holders are, they seldom exercise them, but, instead, usually go along with whatever proceedings have already been instituted. It is the well-known inertia of such security-holders which led to the enactment of many of the provisions of Chapter X. Consequently, it is impossible to believe that Congress intended that, once a petition under Chapter X has been filed by a debtor, the federal court should dismiss it, because of the prior conduct of the debtor in a pending state court proceeding, without regard to whether the interests of the creditors will be as well protected in such prior proceeding—merely on the ground that, if the creditors so desire, they later can themselves, independently, file a petition under Chapter X. Under the reasoning of the majority opinion, the present petition, filed by the debtor, will be dismissed without regard to the interests of the certificate-holders, but if, the next day, three certificate-holders, with claims of $5,000, should be alert enough to file a petition, then the district court would be obliged

to refuse a dismissal because then it would be required to consider the best interests of the creditors and to ignore the prior conduct of the debtor in the state court proceedings. [fol. 125] Surely now that a petition has been filed, although filed by the debtor, the same considerations should apply as if creditors had filed it.

The history of the concept of "good faith" has an important bearing on the interpretation of those words in Section 246: (a) That concept had its origin in the reaction to "friendly" equity receiverships, sometimes used by debtors in conjunction with certain of their creditors, to bring about reorganizations often improperly favorable to the debtor or its management at the expense of other creditors. At a period when the reorganization aspects of such receiverships were still considered not the concern of the courts, and when they still confined their attention solely to the formal aspects of the proceedings,[17] such "collusive" methods of initiating the proceedings were condoned.[18] But *Northern Pacific Ry.* v. *Boyd*, 228 U. S. 482 (1913) ushered in an era, in which the courts exercise jurisdiction to pass upon the fairness and equity of the reorganization plans which were the true objectives of such receiverships. As a result, there later developed a condemnation of the "friendly" or "collusively" begun receivership and a renewed emphasis on the notion that the receiver must be independent, not a representative of the debtor or any class of creditors, but the eyes and ears of the court. Cf. *Harkin* v. *Brundage*, 276 U. S. 36 (1927); *Shapiro* v. *Wilgus*, 287 U. S. 348 (1932); *Natl. Bk.* v. *Flershem*, 290 U. S. 504 (1933).

The increased awareness that the reorganization was the core of such proceedings, led to the enactment of Section 77-B, which created a judicial procedure fashioned expressly for the purpose of reorganization, recognizing squarely that [fol. 126] the fairness, equity and feasibility of the plan were matters directly for the court's consideration. Unfortunately, however, in one important respect, Section 77-B, marked a retrogression from the equity receivership practice: It permitted the debtor to be continued in possession;

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[17] Cf. Cravath, *Reorganization of Corporations*, in Some Legal Phases of Corporate Financing and Regulation (1917) 153, 190-191; *Conley* v. *International Pump Co.*, 237 Fed. 286, 287 (S. D. N. Y. 1915).

[18] *Re Metropolitan Railway Receivership*, 208 U. S. 90.

and it imposed no standards with respect to the disinterestedness of the trustee, in the event that one was appointed. As a result, in actual practice, in many, if not most, cases, the persons in possession of the property were members of the old management. Moreover, consents to a plan under Section 77-B had to be obtained before the plan could be brought before the court for confirmation. This put pressure on the judge not to undo the efforts expended in procuring such consents—often obtained by the old management or those friendly to it and frequently before the proceedings in court were begun—so as to induce the judge to regard consents given by a large percentage of the creditors as substantial evidence of the fairness of the plan and its feasibility. Not until 1939, after Section 77-B had been repealed, did the Supreme Court, in *Case* v. *Los Angeles Lumber Co., Ltd.*, 308 U. S. 106, 114-115, hold that such a criterion under that Section was improper. Meanwhile, many courts had approved plans (on the assumption that a fair plan was to be merely a sort of bargain)[19] which, measured by the rules later laid down in *Case* v. *Los Angeles Lumber Co., supra*, were unduly beneficial to the debtor and unfair to some of its creditors. While that attitude maintained, the intention and motivations of the persons who instituted Section 77-B proceedings were still of considerable importance—of even greater importance, indeed, than under the more recent equity receivership procedure where, at least, the receiver was sure to be disin-
[fol. 127] terested and where the debtor could not remain in possession, so that the power of the old management to play a role in the formulation of the plan was likely to be less than under Section 77-B. The original concept of "good faith" in the initiation of the proceeding, therefore, justifiably remained dominant under Section 77-B.

The defects in the Section 77-B procedures, above noted, were among the principal reasons for the repeal of that Section and the enactment, as a substitute, in 1938, of the provisions of Chapter X. Those provisions eliminated the possibility of consummating plans improperly devised in the interest of the debtor of any special group of creditors. For, once the court takes jurisdiction under Chapter X, the

[19] E.g. *In re A. C. Hotel Co.*, 93 F. (2d) 841 (C. C. A. 7, 1937); *Downtown Investment Ass'n* v. *Boston Metropolitan Buildings*, 81 F. (2d) 314 (C. C. A. 1, 1936).

proceeding ceases to be under the control of the petitioners or the debtor; it is conducted by a disinterested trustee—who must prepare a plan or report why one cannot be effected—under the constant surveillance by the court, usually assisted by the S. E. C.; and no acceptances of any plan, conditional or unconditional, may, without the consent of the court, be solicited until after the entry of an order approving the plan.

The consequence is that even if a Chapter X petition is filed with an improper intent to bring about a plan lacking in fairness to all the creditors or in feasibility, that improper intent can no longer be realized. Therefore, the existence of such an intent on the part of any petitioner—whether the debtor or anyone else—has become utterly irrelevant under Chapter X. "Good faith" does not have an inflexible meaning regardless of context. The original concept of "good faith," meaningful in the equity receivership and Section 77-B cases, has, accordingly, become meaningless under Chapter X.[19a] To import that concept—designed to prevent [fol. 128] harm to creditors resulting from proceedings begun with an improper or "collusive" purpose—into Chapter X, where such harm is now impossible, so as to compel a dismissal of a Chapter X proceeding solely because of some improper purpose on the part of the debtor or other petitioner, is, paradoxically, to do harm to the creditors through the denial to them of the benefits of a sound and equitable reorganization.[20]

Section 246 must be read in the light of Section 256: The latter section provides that prior proceedings may be superseded regardless of the length of time in which they have been pending. The mere pendency of such prior proceedings, consequently, creates no presumption of any lack of "good faith" in the filing of a Chapter X petition. And, in this connection, we should not ignore this fact: *There is the possibility that, to the detriment of creditors, the prior proceeding "may have been resorted to for the purpose of avoiding the protective devices and stringent standards of Chapter X. It is believed that since the enactment of Chapter X, there has been a substantial increase in the use of state rehabilitation procedures formerly thought to be less desirable and*

[19a] Cf. *Snyder* v. *Fenner*, 101 F. (2d) 736.

[20] Cf. 18 N. Y. U. L. Q. Rev. (1941) 399, 415.

efficient than bankruptcy reorganization procedures."[21] *Such state proceedings, it is suggested,*[21a] *have been utilized, to avoid the safeguards of, and supervision under, Chapter X, just as—until the Supreme Court intervened to stop that practice, in S. E. C. v. U. S. Realty and Improvement Co.,* 310 U. S. 434,[22] *Chapter XI proceedings were similarly being employed.*

Let us assume, *arguendo*, that, in the instant case, the state court proceeding was begun and had been acquiesced [fol. 429] in by the debtor for the purpose of avoiding the Chapter X safeguards, but that the debtor, subsequently—but, of course, mistakenly—believing that it would fare better under Chapter X, filed the Chapter X proceeding now before us. There would then be a lack of "good faith," in a colloquial sense, on the part of the debtor. But that bad faith of the debtor in instituting the Chapter X proceeding should surely not operate to take away from the creditors the benefits which they will receive under Chapter X of which, on our assumption, the prior proceeding was designed to deprive them. *Indeed, the more the bad faith of the debtor and those confederating with it in such circumstances, the more reason the bankruptcy court should take jurisdiction.*

There is, then, much merit in the suggestion that such a situation as existed in the *Rembaugh* case and as exists here "would seem to call for the remedies offered by Chapter X," and that "*the interests of the security-holders in a successful and needed rehabilitation should be deemed superior to the possibly questionable motives of the debtor.*"[23]

It should be added that there is no justification for ascribing any unfair motives to the debtor in the instant case. It may have some hopes of supplying new cash so as to permit it or its stockholders to participate in a plan; or it may be desirous of bringing about a plan, fair to its creditors and feasible, in which it will not participate.

For reasons similar to those noted above, it seems plain to me that the doctrine of "election of remedies," intimated in the *Rembaugh* opinion, and by the majority here should

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[21] *Ibid*, 417 and note 161.

[21a] *Ibid.*

[22] Reversing the decision of this court in *In re U. S. Realty and Improvement Co.*, 108 F. (2d) 794.

[23] N. Y. U. L. Q. Rev. *supra*, 418.

be given no weight. That harsh doctrine is fast becoming weaker even in its traditional strongholds,[24] and I cannot [fol. 130] acquiesce in the attempt to import it into the streamlined procedure of the Chandler Act. A Chapter X procedure is not a piece of litigation in which the debtor is one of the contending parties, a lawsuit in which it seeks relief against someone else. As Judge Lindley said of an equity receivership reorganization proceeding, it "is of necessity largely administrative" and requires "the exercise of administrative jurisdiction, as distinguished from decision of controverted or litigated questions."[25] The debtor filing such a petition is not a plaintiff commencing an action; if the court takes jurisdiction, an administrative proceeding ensues in which the estate is administered by an independent trustee under the court's supervision. "Election of remedies" is a doctrine wholly alien to such non-litigious atmosphere.

Even if the doctrine were applicable, I cannot understand why any such election of remedies by the debtor should be determinative of what is for the best interests of the creditors. Again, viewing the situation realistically, it is obvious that the certificate-holders themselves have not, in any real sense, elected in favor of the state court proceeding. They did not select the trustee which now favors the state proceedings, nor can it be realistically said that they have ratified its appointment or actions. The trustee's claim that it can arbitrarily restrict the certificate-holders to the state court proceeding is especially surprising since, so far as appears, the trustee has given them no notice of the present action, and since, in the Chapter X proceeding to which the trustee objects, they will be entitled to notice and a hearing on the appointment of a Chapter X [fol. 131] trustee, 11 U. S. C. A. 561, 562, as well as to vote on a proposed plan, 11 U. S. C. A. 579. And even if it could be said that the certificate-holders had acquiesced in the prior

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[24] See Clark, *Code Pleading* (1928) 335-339; Hinc, *Election of Remedies, a Criticism* (1913) 26 Harv. L. Rev., 707; Comment (1925) 34 Yale L. Rev. 665.

[25] *Lincoln Printing Co.* v. *Middle West Utilities Co.*, 6 Fed. Supp. 663, 682-683; cf. S. E. C., *Report on the Study and Investigation of the Work, Activities, Personnel and Functions of Protective and Reorganization Committees*, Part VIII, 1-2.

proceeding, nevertheless, no theory of election or estoppel should control since, under Clause (4), the inquiry must be what is for their best interests. That cannot be determined by whether or not they acquiesced in the prior proceedings, since Congress indicated no such factor as a test of what is for their best interests.

For the foregoing reasons, we should affirm the order of the district court refusing to dismiss the petition. At most, we should either (a) direct the district court to vacate its order and dismiss the petition, if, and only if, appellant satisfies the district court that some persons interested in the estate have relied to their detriment on the ruling in the *Rembaugh* case;[26] or (b) announce that hereafter, absent proof of such reliance, we shall not adhere to that ruling.[27]

[fol. 132] UNITED STATES CIRCUIT COURT OF APPEALS,
SECOND CIRCUIT

At a Stated Term of the United States Circuit Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the 27th day of January, one thousand nine hundred and forty-two.

Present: Hon. Thomas W. Swan, Hon. Harrie B. Chase, Hon. Jerome N. Frank, Circuit Judges.

In the Matter of MARINE HARBOR PROPERTIES, INC., Debtor,

MANUFACTURERS TRUST COMPANY, as Trustee, etc., Appellant

Appeal from the District Court of the United States for the Southern District of New York

This cause came on to be heard on the transcript of record from the District Court of the United States for the Southern District of New York, and was argued by counsel.

On consideration whereof, it is now hereby ordered, adjudged, and decreed that the order of said District Court be and it hereby is reversed with costs.

It is further ordered that a Mandate issue to the said District Court in accordance with this decree.

D. E. Roberts, Clerk.

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[26] See authorities cited in footnote 1.

[27] See authorities cited in footnote 2.

[fol. 133] [Endorsed:] United States Circuit Court of Appeals, Second Circuit. In the Matter of Marine Harbor Properties, Inc. Order for Mandate. United States Circuit Court of Appeals, Second Circuit. Filed Jan. 27, 1942. D. E. Roberts, Clerk.

[fol. 134] UNITED STATES OF AMERICA,
Southern District of New York:

I, D. E. Roberts, Clerk of the United States Circuit Court of Appeals for the Second Circuit, do hereby certify that the foregoing pages, numbered from 1 to 133, inclusive, contain a true and complete transcript of the record and proceedings had in said Court, in the case of In the Matter of Marine Harbor Properties, Inc., Debtor, Manufacturers Trust Company, as Trustee, etc., Appellant, as the same remain of record and on file in my office.

In testimony whereof, I have caused the seal of the said Court to be hereunto affixed, at the City of New York, in the Southern District of New York, in the Second Circuit, this twenty-seventh day of January, in the year of our Lord one thousand nine hundred and forty-two, and of the Independence of the said United States the one hundred and sixty-sixth.

D. E. Roberts, Clerk. (Seal.)

SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed March 16, 1942

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

No. ~~948~~ 24

MARINE HARBOR PROPERTIES, INC.,

Petitioner,

vs.

MANUFACTURER'S TRUST COMPANY, (successor by merger to the Mortgage Corporation of New York), as trustee for the benefit of certificate holders in mortgage guaranteed by Bond & Mortgage Guarantee Company, Guarantee #181,568,

MAURICE RUBINGER, trustee of Marine Harbor Properties, Inc.,

SAMUEL SIVERMAN, additional trustee of Marine Harbor Properties, Inc.,

MORTIMER RUBENSTEIN, Foreclosure-receiver,

and

SECURITIES AND EXCHANGE COMMISSION.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

FRIEDLAND & FRIEDLAND,
Counsel for Petitioner,
Marine Harbor Properties, Inc.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

MARINE HARBOR PROPERTIES, INC.,
Petitioner,

vs.

MANUFACTURER'S TRUST COMPANY, (successor by merger to the Mortgage Corporation of New York), as trustee for the benefit of certificate holders in mortgage guaranteed by Bond & Mortgage Guarantee Company, Guarantee #181,568,

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SECURITIES AND EXCHANGE COMMISSION.

No.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

TO THE HONORABLE, THE CHIEF JUSTICE AND THE ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

Your petitioner, Marine Harbor Properties, Inc., (the Debtor herein), a corporation organized under the laws

of the State of New York, prays this Court for the issuance of a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit to review a decree of that Court entered January 27, 1942, reversing an order of the United States District Court for the Southern District of New York, denying an application by The Mortgage Corporation of New York, as trustee for mortgage certificate holders, to dismiss the Debtor's petition for reorganization under Chapter X of the Bankruptcy Act and to vacate its order approving the Debtor's petition.

Opinions Below.

The opinion of the District Court is part of the record (R. 70-75) and is also reported in 41 F. Supp. 814 (S. D. N. Y.), advance sheets. The majority and dissenting opinions of the Circuit Court of Appeals are not yet reported but are contained on pages 107 to 131 of the record.

Jurisdiction.

The decree of the Circuit Court of Appeals was entered January 27, 1942. The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925.

Questions Presented.

1. Whether the relief afforded by Chapter X of the Bankruptcy Act must be denied to a mortgagor-debtor and its mortgage certificate holders merely because, some six years prior to the filing of the Chapter X petition, a modification and extension of the certificated mortgage on the Debtor's property was consented to by a state court

in proceedings conducted under the provisions of the Schackno Act (Chapter 745 of the New York Laws of 1933, as amended) and the Mortgage Commission Act (Chapter 19 of the New York Laws of 1935).

2. Whether a Debtor's petition for reorganization under Chapter X may be dismissed pursuant to Section 146(4) thereof as not having been filed in good faith, without determining whether the interests of security holders would be best subserved in prior state court proceedings, and without a showing that a procedure is available in such proceedings providing security holders with safeguards substantially equivalent to those provided by Chapter X.

3. Whether, if good faith is not lacking pursuant to Section 146(4) of Chapter X, a finding of lack of good faith in the filing of a Debtor's petition may be predicated upon an alleged personal disqualification of the Debtor arising out of previous participation in prior state court proceedings.

Statutes Involved.

The statutes involved are the following provisions of the Bankruptcy Act:

Section 141 (11 U. S. C. §541): "Upon the filing of a petition by a debtor, the judge shall enter an order approving the petition, if satisfied that it complies with the requirements of this chapter and has been filed in good faith, or dismissing it if not so satisfied."

Section 146 (11 U. S. C. §546): "Without limiting the generality of the meaning of the term 'good

faith, a petition shall be deemed not to be filed in good faith if— * * * (4) a prior proceeding is pending in any court and it appears that the interests of creditors and stockholders would be best subserved in such prior proceeding.'"[1]

Statement.

The Debtor's principal asset is an apartment building in New York City. The first mortgage on its property was originally held by The Title Guarantee & Trust Company, which sold participation certificates to the public, guaranteed as to principal and interest by Bond & Mortgage Guarantee Company. (R. 8)

In 1933, the Superintendent of Insurance of the State of New York, pursuant to an order of the Supreme Court of the State of New York, took possession, as Rehabilitator, of the property and business of Bond & Mortgage Guarantee Company. (R. 8, 9) Thereafter, acting under powers granted to him by the Schackno Act, the Superintendent of Insurance, with the approval of certificate holders and the state court, effectuated a modification and extension of the terms of the first mortgage on the Debtor's property, which, by agreement executed between the Debtor and Title Guarantee & Trust Company in 1935, extended the maturity of the mortgage to 1937, and re-

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[1] In the court below it was also argued that a finding of lack of good faith should have been made by the District Court because of Section 146(3) (11 U. S. C. §546 [3]) which reads:

"Without limiting the generality of the meaning of the term 'good faith', a petition shall be deemed not to be filed in good faith if— * * * (3) it is unreasonable to expect that a plan of reorganization can be effected".

The Circuit Court of Appeals correctly rejected this argument. (R. 110-111) On this point, Circuit Judge Frank, who dissented, was in complete accord with the majority of the Court (See his opinion at R. 117).

duced the interest thereon from 6% per annum to 5% per annum. (R. 11) In 1938, at the instance of the Mortgage Commission of the State of New York, (as successor to the Superintendent of Insurance under the Mortgage Commission Act), title to the aforesaid bond and mortgage was transferred, with the consent of certificate holders and the state court, to The Mortgage Corporation of New York as trustee for certificate holders under a Declaration of Trust which vested the mortgage trustee with enumerated powers to manage and control the trust estate until it is fully liquidated. (R. 38-44) In giving its consent, the state court expressly reserved jurisdiction to grant other relief on the application of "the trustee, or any other interested party". (R. 44) Manufacturers Trust Company is successor by merger to The Mortgage Corporation of New York. (R. 3)

The principal of the first mortgage was not paid at maturity and remained unpaid under the statutory moratorium.[1] The Debtor made all other payments until April, 1941, when it defaulted on interest and taxes. (R. 12) In May, 1941, the trustee commenced foreclosure proceedings and a receiver was appointed therein. (R. 12, 13) The Debtor, on several occasions, both before and after foreclosure, offered the trustee various proposals to further extend and modify the mortgage but the trustee never submitted any of such proposals either to the state court or to the certificate holders. (R. 13, 14)

On September 17, 1941, the Debtor filed its petition for reorganization under Chapter X. (R. 76) The petition was approved, and reorganization trustees were appointed by the District Court. (R. 96) The Mortgage Corporation of New York, as trustee, thereafter applied

[1] In 1933 foreclosure for principal defaults was suspended in the State of New York for an emergency period. (Chapter 793 of the New York Laws of 1933) The emergency period has been extended by amendments from time to time thereafter enacted and now expires July 1, 1943. (Chapter 782 New York Laws of 1941)

to the District Court to vacate its order of approval and dismiss the petition as not filed in good faith. (R. 7-21) The application was denied (R. 4-5) and an appeal from the order denying the application was taken by the mortgage trustee to the United States Circuit Court of Appeals for the Second Circuit. The Circuit Court, in a divided opinion, reversed the order of the District Court.

Specification of Errors to be Urged.

The majority of the Court below erred:

1. In holding that the Debtor's petition for reorganization under Chapter X of the Bankruptcy Act, was not filed in good faith.

2. In holding that there was an absence of good faith on the part of the Debtor because the Debtor had assented to a modification and extension of a certificated mortgage in a state court proceeding.

3. In failing to determine whether or not the interests of creditors and stockholders would be better subserved in the state court proceedings than in proceedings under Chapter X of the Bankruptcy Act, and whether or not such state court proceedings would provide for public investors safeguards equivalent to those provided by Congress in Chapter X.

4. In holding that the state court proceedings under the Schackno and Mortgage Commission Acts were "prior pending proceedings" within the meaning of Section 146(4) of Chapter X.

5. In failing to affirm, and in reversing, the order of the District Court.

Reasons for Granting the Writ.

The decision below is one of several cases decided by the United States Circuit Court of Appeals for the Second Circuit, all of which dealt with the effect of prior state court proceedings on the issue of a Debtor's good faith in the filing of a petition under Chapter X of the Bankruptcy Act. See *Brooklyn Trust Co.* v. *Rembaugh*, 110 F. (2d) 838; *In re Blinrig Realty Corp.*, 114 F. (2d) 100; *In re Castle Beach Apartments, Inc.*, 113 F. (2d) 762.[1] In all the cases cited, as well as in the present case, the question of good faith was resolved by the Circuit Court in terms of an alleged personal disqualification of the particular Debtor who attempts to resort to Chapter X of the Bankruptcy Act after participating in a prior state court proceeding instituted by other persons. The Circuit Court's rationale in the cases cited has been the subject of a good deal of adverse comment. See 18 N. Y. U. L. Q. Rev. (1941) 399, 411-413, 417-418; Siegel, *Chapter X or Schackno Act Proceedings?* (1941) 27 Corn. L. Q. 56.

The Court below concedes that in these cases there is no doubt of the jurisdiction of the District Court to entertain the Debtor's petition notwithstanding prior proceedings in a state court.[2] See *Brooklyn Trust Co.* v. *Rembaugh*, *supra*, at p. 840. The only concern of the

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[1] There have also been similar cases not reported in the Circuit Court of Appeals. See *In re 263 West 38th Street Corp.*, 37 F. Supp. 661; *In re Paloma Estates, Inc.*, C. C. H. Bankr. Serv. par. 53,336, now pending on appeal in the Circuit Court of Appeals for the Second Circuit.

[2] Section 256 of Chapter X (11 U. S. C. §656), expressly provides:

"A petition may be filed under this Chapter notwithstanding the pendency of a prior mortgage foreclosure, equity, or other proceeding in a court of the United States or of any State in which a receiver or trustee of all or any part of the property of a debtor has been appointed or for whose appointment an application has been made."

Circuit Court has been as to the propriety of the District Court's taking jurisdiction. The exercise of discretion by the District Court in approving the Debtor's petition here was overruled by the majority of the Circuit Court merely because of the prior state court proceedings and the Debtor's conduct therein. The reason for so doing was stated by the Court below thus:

> "In the *Rembaugh* case we held the element of good faith to be lacking because a debtor, which had voluntarily submitted to a plan for reorganization in the state court but found compliance therewith irksome, invoked federal jurisdiction instead of seeking relief in the state court. * * * A majority of the court is of the opinion that the *Rembaugh* case should be given effect here to prevent a debtor, who has assented to a plan which is being supervised by the state court in reorganization proceedings still pending there, from flouting that jurisdiction by filing a petition in the district court. The applicable principle, as was said in the *Rembaugh* case, is not an absence of good faith in the filing of the new petition in the broad meaning of those words but a special instance of a lack of good faith flowing from the personal disqualification of the debtor. Section 146 (11 U. S. C. A. §546) expressly disclaims any limitation upon the generality of the meaning of good faith and subsection 4 of that section is but one special instance of what will show a disabling absence of it on the part of a debtor *and is not to be confused with what controls here.*" (Italics added) (R. 112, 113)

It is not clear from the language of the majority of the Circuit Court whether its holding rests on Section 146(4) of Chapter X or on a concept of good faith not expressly defined in Section 146, although Circuit Judge Frank,

dissenting, assumed that the decision, in part at least, rests on Section 146(4). (R. 113) The resulting ambiguity requires consideration of the Circuit Court's determination from both viewpoints. We believe neither is tenable in this case.

1. The state court proceeding, which is present in this case, does not meet the requirements of Section 146(4) so as to justify the dismissal of the Debtor's petition. That section provides for a dismissal of a Debtor's petition as not filed in good faith when it appears that there is another proceeding pending in any court wherein "the interests of creditors and stockholders would be best subserved". We submit that the state court proceedings in this case do not meet this standard in comparison with the power and safety devices provided by proceedings under Chapter X of the Bankruptcy Act, and therefore should not be permitted to bar a federal reorganization.

The limitations on the *power* of the state court proceeding are exemplified in the necessity of the state court trustee to institute foreclosure proceedings to wipe out the Debtor's title to its property; the need to institute a separate and wholly independent action to cope with fraud and dishonesty (*cf. Weil v. President, etc.*, 275 N. Y. 238); and the absence of any right in the creditors to investigate the Debtor's past management, or its future prospects. However, in a federal reorganization under Chapter X of the Bankruptcy Act none of these limitations is to be found. Title to the Debtor's property vests in the reorganization trustee immediately upon his qualification as such (Section 186). And once the Court assumes jurisdiction, the disinterested trustee has the power not only to investigate the Debtor's past management, (indeed it is his duty to do so under Section 167) but power to take action against the Debtor for fraud and

mismanagement, since he possesses all of the powers of a bankruptcy trustee (Section 187).

In the matter of *safety*, there are many reasons why the federal proceeding is superior to state reorganizations. In the first place, the doctrine of absolute priorities, enunciated in *Case* v. *Los Angeles Lumber Products Co.*, 308 U. S. 106, is applicable in Chapter X, but finds no currency in state court reorganizations. Secondly, the structure of Chapter X offers protective devices in cases where the liabilities exceed $250,000, as in this case, that are wholly absent in the state courts.

The reorganization trustee and his attorney must be disinterested (Sections 156-8). The reorganization trustee, upon appointment and qualification, must investigate the property, the Debtor's prior management and operation of the property, and the desirability of its continuance (Section 167[1]). The trustee must also report to the judge any fraud, misconduct or mismanagement (Section 167[3]). The results of these investigations are then sent to creditors and stockholders, who are asked to suggest proposals to be included in a plan (Section 167[5],[6]). Before approving a plan, the District Court may seek the aid of the Securities and Exchange Commission for an advisory report (Section 172). A hearing on a plan is then had, on notice to creditors and stockholders (Section 171). Solicitation of acceptances to a plan is prohibited until after the District Court approves the plan (See Section 176). The District Court, before approving a plan, must inquire as to its fairness, examine into the new capital structure; make a finding that the earning capacity of the new enterprise will be sufficient to meet fixed charges; determine that the distribution of new securities (if no cash settlement is made) reflects existing rights and are equitably treated. (*Case* v. *Los Angeles Lumber Co., supra*, at p. 115; *Consolidated Rock Products Co.* v. *DuBois*, 61 Sup. Ct. 675) After the plan

is thus scrutinized by the District Court, usually assisted by the Securities and Exchange Commission, it is submitted, with other available data and reports, to the interested parties for their consideration (Section 175). When the plan has been accepted by the necessary majorities, a hearing is held for its confirmation upon due notice to all creditors and stockholders (Section 179). If the plan is fair, equitable and feasible, and if its proposal and acceptance are in good faith and not in violation of any of the prohibitions contained in the Act, it will be confirmed (Section 221[2]). The Court's investigation does not stop here but is directed even to the methods by which the management of the reorganized corporation is to be chosen in order to insure adequate representation for the interests of all creditors and stockholders (Section 221[5]). To that end, the District Court may pass upon the qualifications of the management and voting trusts, if any, upon the consummation of the plan (Section 216[11]).

In all of these ways every possible safeguard is provided for the protection of every class. The Schackno Act, on the other hand, does not provide for corresponding safeguards. Particularly is it lacking in a device whereby the creditors, secured or unsecured, and the stockholders can receive a full and impartial report from a disinterested trustee. It is contended that in state court procedures there is such a safeguard in the form of the Bureau of Trust Supervision, an agency allegedly created by Chapter XIX of the Laws of 1940, New York, amending Section 17-a of Chapter XIX of the Laws of 1935, New York. However, the record fails to disclose any evidence showing the nature of the duties and obligations of this alleged agency, the facilities it has to properly assist and advise the Court and creditors on proposed plans, or a history of achievement in the field of reorganization.

For all of the above reasons it is respectfully submitted that the state court proceeding, present in this case, does not meet the requirements of Section 146(4) in that it does not appear that therein the interests of creditors and stockholders will be best subserved.

2. The Debtor's prior conduct in the state court does not disqualify it from reorganization in the federal court. The decision of the majority of the Circuit Court below holds, in effect, that the Debtor herein is forever bound to remain in the state court. This disqualification is based on the Debtor's agreeing, some 6 years ago, to a modification and extension of its mortgage in the State proceeding. Therefore, the Circuit Court would deny this Debtor, or any Debtor who had ever invoked, or had otherwise been subject to, the jurisdiction of the state court, the right to enter the federal court for the purpose of reorganizing. And this disqualification would attach to every Debtor, regardless of any change in circumstances. Neither would it matter that the State procedure would not best subserve the interests of creditors and stockholders. Neither would the absence of any pending State procedure assist in opening the doors of the federal court to a distressed Debtor. The only test to be applied, according to the Circuit Court below, is—did the Debtor ever voluntarily submit, or was it ever subject to, the jurisdiction of the state court? If so, then the federal court is to remain forever closed to such a Debtor and the remedies of Chapter X are to remain unavailable.

Far from being disqualified by its participation in the state court proceedings, the Debtor, in this case, should be welcomed into the federal court. For the Debtor herein, on several occasions, entered into negotiations looking to a further modification of its mortgage, but the trustee of the certificate holders declined the Debtor's

several proposals after submitting them only to its Trust Committee. "No submission of the proposed modification was made either to the Court or to the certificate holders" (opinion of District Court, R. 72). The Debtor was thus "rebuffed by the trustee and has had no opportunity to make application for the relief which obviously the situation requires" (opinion of District Court, R. 73).

It seems clear that, particularly in this case, the Debtor should not be held personally disqualified from entering the federal court after being summarily rebuffed by the trustee of the certificate holders. The Circuit Court below would ignore, however, this *impasse* and hold that having been subject to the jurisdiction of the state court, six years back, the Debtor is bound to remain there.

We think that this holding is narrow, unjust, and in direct conflict with the intention of Congress when enacting Chapter X. When the Chandler Act was enacted in 1938, there was hardly one mortgage guaranty company (which had sold mortgage participation certificates to the general public) that was not in some stage of rehabilitation or liquidation in the state courts.(4) At one time or another, since the advent of the depression that followed 1929, every Debtor of these mortgage guaranty companies voluntarily submitted, or was otherwise subject, to the jurisdiction of the state court. Thus, if the holding of the Circuit Court is permitted to stand, Federal treatment of this entire situation, on the Debtor's application, would be forever barred for the simple reason that every Debtor of mortgage guaranty companies is personally disqualified to do so.

(4) In New York State alone, the corpus of existing guaranty certificated mortgages exceeded in value $700,000,000. In this corpus over 200,000 persons held participating interests. *Report to His Excellency, Herbert H. Lehman, Governor of the State of New York, by George W. Alger, dated October 5, 1934, on p. 5.*

Conclusion.

Section 146(4) refers to a situation in which good faith will be presumed absent if there is a "prior proceeding pending wherein it appears that the interests of creditors and stockholders would be best subserved". No other standard, such as the Debtor's alleged personal disqualification, was provided by Congress to justify a finding of an absence of good faith under this subdivision. Nevertheless, the Circuit Court below undertook to deny to creditors and stockholders the protective devices of Chapter X, and the beneficial results that were to be derived from its application, because of the alleged personal disqualification deemed to exist on the part of the Debtor.

Thus the objective standard of bad faith, as defined by Section 146(4), appears to have been replaced by a new and subjective standard, not provided for therein. As a consequence the majority of the Circuit Court failed to determine directly whether or not the state court proceeding was one wherein the interests of creditors and stockholders would be best subserved. That question is of tremendous importance to the real estate mortgage situation which, since 1929, has afflicted our country. It is today a Federal question which should be, but has not been, decided by this Court.

Wherefore, petitioner prays that this petition for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit, should be granted.

Dated: February 11th, 1942.

Friedland & Friedland,
Counsel for Petitioner,
Marine Harbor Properties, Inc.

State of New York, }
County of New York, } ss.:

SOL FRIEDLAND and ARTHUR E. FRIEDLAND, being duly sworn, depose and say, that they are counsel for the petitioner named in the foregoing petition. That they prepared the same and that the allegations thereof are true as they thoroughly believed.

SOL FRIEDLAND.
ARTHUR E. FRIEDLAND.

Subscribed and sworn to before me this
11th day of February, 1942.

MURRAY WALDMAN,
Commissioner of Deeds, New York City,
Term Exp. June 11, 1942,
N. Y. County Clerk's #56.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

No. 948 24

MARINE HARBOR PROPERTIES, INC.,
Petitioner,

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MANUFACTURER'S TRUST COMPANY, (successor by merger to the Mortgage Corporation of New York), as trustee for the benefit of certificate holders in mortgage guaranteed by Bond & Mortgage Guarantee Company, Guarantee #181,568,

MAURICE RUBINGER, trustee of Marine Harbor Properties, Inc.,

SAMUEL SILVERMAN, additional trustee of Marine Harbor Properties, Inc.,

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and

SECURITIES AND EXCHANGE COMMISSION.

BRIEF IN SUPPORT OF PETITIONER.

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Marine Harbor Properties, Inc.

MARK SERVICE, BARCLAY 7-2180

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and

SECURITIES AND EXCHANGE COMMISSION.

No. 948.

BRIEF IN SUPPORT OF PETITIONER.

Opinions Below.

The opinion of the District Court is contained in the record (R. 70-75). It is also reported in 41 Fed. Supp. 814 (S. D. N. Y.). The majority and dissenting opinions of the Circuit Court of Appeals are contained on Pages 107 to 131 of the record. They are also reported in 125 Fed. (2) 296 (advanced sheets).

Jurisdiction.

The jurisdiction of this court is invoked under Section 240 (A) of the judicial code as amended by the Act of February 13, 1925.

Statement.

The debtor is a New York corporation whose principal asset is an apartment building in New York City. Encumbering said asset is a first mortgage, which was originally held by the Title Guarantee and Trust Co., but this corporation sold it to the general public through certificates of participation therein. Payment of the principal and interest of said certificates of participation was guaranteed, however, by Bond & Mortgage Guarantee Co. (R. 8), also a New York corporation.

The depression that followed 1929 resulted in the insolvency of Bond & Mortgage Guarantee Co. In 1933, the Superintendent of Insurance of the State of New York, pursuant to an order of the Supreme Court of the State of New York, took possession of the property and business of the said Bond & Mortgage Co., in order to rehabilitate same (R. 8-9). Thereafter, the Superintendent of Insurance, acting under powers granted to him by the Schackno Act of the State of New York (Chap. 745, New York Laws, 1933), and with the approval of certificate holders and the State Court extended the maturity date of the said first mortgage and reduced the interest thereon from 6% to 5% per annum (R. 11).

In 1938, the Superintendent of Insurance was succeeded (R. 38-44) by the Mortgage Corporation of New York, who, pursuant to an order of the State Court, made and delivered a Declaration of Trust (R. 23-37). By the terms

of this instrument, there was vested in the said Mortgage Corporation of New York, certain enumerated powers to manage and control the first mortgage investment until it was fully liquidated (R. 38-44). When the said Declaration of Trust was approved, the State Court expressly reserved jurisdiction to grant other relief on the application of "the trustee or any other interested party" (R. 44). The respondent, Manufacturers' Trust Co., is the successor-by-merger of the Mortgage Corporation of New York (R. 3).

The principal of the first mortgage was not paid by the debtor at maturity and still remains unpaid, but foreclosure, because of said non-payment of principal, was suspended by special acts of the New York State Legislature. (Chap. 500, New York Laws 1938; Chap. 606, New York Laws 1939; Chap. 566, New York Laws 1940; Chap. 782, New York Laws 1941). The debtor remained in possession of its property and made all other payments until April, 1941, when it defaulted on interest and taxes (R. 12).

Upon such default, the Mortgage Corporation of New York commenced foreclosure proceedings (R. 12-13). During the pendency of those proceedings, the debtor offered the Mortgage Corporation of New York various proposals to extend and modify the terms of the mortgage, but these various proposals were rejected (R. 14). They never reached the State Court or the certificate holders for their consideration (R. 72).

On September 17, 1941, the debtor filed an *ex parte* petition for reorganization under Chapter X (R. 76). The petition was approved and reorganization trustees were appointed by the District Court (R. 96). The Mortgage Corporation of New York thereafter applied to the District Court to vacate the *ex parte* order of approval and to dismiss the petition as not filed in good faith (R. 7-21). This application was denied (R. 4-5) and an appeal (R. 3)

from the order denying such application was taken by the Mortgage Corporation of New York to the United States Circuit Court of Appeals for the Second Circuit. By a divided bench (R. 107-126), the Circuit Court reversed (R. 126) the order of the District Court.

Specifications of Errors to be Urged.

The majority of the Court below erred:

1. In holding that the Debtor's petition for reorganization under Chapter X of the Bankruptcy Act was not filed in good faith.

2. In holding that there was an absence of good faith on the part of the debtor because the debtor has assented to a modification and extension of a certificated mortgage in a State Court proceeding.

3. In failing to determine that the interests of creditors and stockholders would be better subserved in the State Court proceedings than in proceedings under Chapter X of the Bankruptcy Act, and that such State Court proceedings would not provide for public investors safeguards equivalent to those provided by Congress in Chapter X.

4. In holding that the State Court proceedings under the *Schackno Act* (Chap. 745, New York Laws of 1933) and the *Mortgage Commission Act* (Chap. 191 New York Laws of 1935) were "prior pending proceedings" within the meaning of *Section* 146 (4) of Chapter X.

5. In failing to affirm, and in reversing the order of the District Court.

Argument.

A summary of the points which are hereinafter made on behalf of the petitioner are:

I. The District Court properly refused to find that there were any prior pending proceedings wherein the interest of creditors and stockholders would be best subserved because (1) Schackno proceedings do not possess the power and safety of a proceeding under Chapter X, (2) they are not now "pending", and (3) in any event the respondent had the burden of proving that they would best subserve the interests of creditors and stockholders which burden the respondent has failed to sustain.

II. The debtor is not personally disqualified from invoking the jurisdiction of the Federal court under Chapter X of the Bankruptcy Act because the debtor never really invoked, or submitted to the jurisdiction of the state court, the debtor has no real standing in Schackno proceedings, and the debtor, as such, was never reorganized in, and is not now being supervised by the state court.

III. The Doctrine of Comity has no application to this case because the National Bankruptcy Act is paramount and superior to any local or state insolvency law, and the debtor has an absolute right to have its property administered under the Bankruptcy Act.

IV. Regardless of the personal disqualification of the debtor, it was error to dismiss its petition for reorganization in the interest of creditors because the protection of creditors' rights is superior to the interests of stockholders and no theory of estoppel or election of remedies should be permitted to deprive creditors of what is in their best interests.

POINT I.

The District Court properly refused to find that there was any prior pending proceedings wherein the interest of creditors and stockholders would be best subserved.

1. *Schackno proceedings do not possess the power and safety of a proceeding under Chapter X of the Bankruptcy Act.*

Schackno proceedings in the State of New York were born out of the depression that followed 1929. They were instituted to rehabilitate or liquidate various bond and mortgage companies that had become insolvent and defunct. They were special proceedings begun under a special act of the New York State Legislature, Chap. 745 New York Laws of 1933, and they became known as Schackno proceedings. They were always commenced by the State Superintendent of Insurance. The principal purpose of these proceedings was to protect the creditors of these insolvent and defunct bond and mortgage companies. Subdivisions 1 of the Schackno Act, *supra*. Thus it was the primary duty of the State Superintendent of Insurance (who has since been supplanted through various steps by the present respondent, sometimes referred to also as "Schackno Trustee") to administer, under the Schackno Act, *supra*, the mortgage investments of these defunct bond and mortgage companies in which groups of investors were interested, *People* vs. *Title & Mortgage Guarantee Co.*, 264 New York 69, at p. 92. In this way, Schackno proceedings were limited in their original nature, and in the extent of their jurisdiction. To date, there has been no change in or enlargement of their nature or the scope of their jurisdiction. They still suffer, as we shall show, from limitations in inherent power to

deal with situations and problems not within their purpose or jurisdiction.

Thus, in Schackno proceedings, property in the possession of the Superintendent of Insurance is not in *custodia legis*. *Acken* vs. *New York Title & Mortgage Co.*, 9 Fed. Supp. 521. A Schackno trustee does not ever acquire title to the property in which he is interested except through foreclosure or conveyance. Nor is a Schackno trustee, in Schackno proceedings, able to cope with a debtor's fraud or dishonesty. To do so, a wholly independent action must be instituted. *Weil, et al.* vs. *President and Directors of Manhattan Co.*, 275 New York 238. Neither does the Schackno trustee possess power to investigate and probe the debtor as to its past management or its future prospects. He remains as he was created, a purely statutory trustee, possessing only such power and authority as is conferred upon him by statute. *Weil, et al.* vs. *President, etc., supra*. *Wolff* vs. *Mortgage Commission, et al.*, 270 New York 428. Furthermore, in a Schackno proceeding, the Court cannot and does not possess jurisdiction over other creditors or junior lienors.

By contrast, the power and jurisdiction of a Chapter X proceeding stand out in bold relief. For when a debtor files a petition for reorganization, title to its property is immediately in *custodia legis*, thereafter vesting in the reorganization trustee upon his qualification as such (*Section 186*). Foreclosure thus becomes unnecessary. And if the debtor be dishonest or its officers be guilty of dishonesty, turn-over proceedings to recover the fruits of such dishonesty may be instituted within the very frame-work of a Federal reorganization. To investigate the debtor, its past management, and future prospects, the trustee has not only the power, but the affirmative duty to do so. (*Section 167*). Furthermore, it is beyond question that, in a Chapter X proceeding, the rights of all parties may be comprehensively examined, considered and dealt with.

Beyond these differences in inherent *power* as between a Chapter X proceeding and a Schackno proceeding, there are differences also in the nature and number of their *safety devices*. For the structure of Chapter X offers and provides protective devices (in cases where the liabilities exceed $250,000 as in this case) that are wholly absent in the state court reorganizations. These features are inherent in the nature and character of a Federal reorganization.

Thus, the reorganization trustee and his attorney must be disinterested (*Sections 156-8*). Upon appointment and qualification, he must investigate the debtor's property, the debtor's past management and operation, and the desirability of its continuance (*Section 167 (1)*). The trustee must also report to the court any fraud, misconduct or mismanagement (*Section 167 (3)*). The results of these beneficial investigations must then be sent to creditors and stockholders, who, upon such information, are asked to suggest proposals to be included in a plan (*Section 167 (5) (6)*). Before approving any plan, the District Court may seek the aid of the Securities and Exchange Commission for an advisory report (*Section 172*). Then, a hearing on a plan is had, on notice to all creditors and stockholders (*Section 171*). Solicitation of acceptances to a plan is prohibited until the District Court has approved the plan (See *Section 175*). And the District Court, before approving any plan, must first inquire as to its fairness, feasibility, and equitability. If no cash settlement is made, the court must examine into the new capital structure; make a finding that the earning capacity of the new enterprise will be sufficient to meet fixed charges; determine that the distribution of new securities reflects existing rights and are equitably treated. *Case* vs. *Los Angeles Lumber Co.*, 208 U.S. 106; *Consolidated Rock Products Co.* vs. *DuBois*, 61 Sup. Ct. 675. Then after all of this preliminary work has been accomplished

and the plan has been thus scrutinized by the District Court, (which is usually assisted by the Securities and Exchange Commission) it is submitted, with other available data and reports, to the interested parties, for their consideration (*Section 175*). When the plan has been accepted by the necessary majorities, a hearing is held for its confirmation upon due notice to all creditors and stockholders (*Section 179*). If the plan is fair, equitable and feasible, and its proposal and acceptance are in good faith and not in violation of any of the prohibitions contained in the Act, it will be confirmed (*Section 221 (2)*). Still, the Courts' investigation does not stop. It is even directed to the methods whereby the management and personnel of the reorganized corporation are to be chosen in order to insure adequate representation for the interests of all creditors and stockholders (*Section 221 (5)*). To that end, the District Court may pass, after the consummation of the plan, upon the qualifications of the management, personnel and voting trustees, if any (*Section 216 (11)*). In all of these ways, every possible conceivable safeguard has been provided by Congress for the protection of every class.

The Schackno Act, on the other hand, does not provide for corresponding safeguards. Particularly is it lacking in a device whereby creditors, secured or unsecured, as well as the stockholders, must receive a full and impartial report from a disinterested trustee, or the Security and Exchange Commission.[1] Neither is there a requirement

[1] It is contended that in state court procedures, there is such a safeguard in the form of the Bureau of Trust Supervision, an agency allegedly created by Chapter 740 of the Laws of 1940, New York, amending Section 17-a of Chapter 19 of the Laws of New York, 1935. However, the record fails to disclose any evidence showing the nature of the duties and obligations of this alleged agency, the facilities it has to properly assist and advise the Court and creditors on proposed plans, or a history of achievement in the field of reorganization.

that a plan must receive the preliminary approval of the court before consents may be solicited. Nor is there a provision for the mandatory application of the doctrine laid down in *Case* vs. *Los Angeles Lumber Products Co., supra.*

But beyond these limitations in the inherent jurisdiction, power and safety of Schackno proceedings is the plain fact that such proceedings, however good they may be, concern themselves solely with the assets of, and claims against insolvent and defunct guaranty companies. Schackno proceedings do not, nor can they, concern themselves with the problems of other debtors, such as the debtor herein, and the junior lienors. Thus, a person owning a chattel mortgage on the property of the debtor is not considered to be, nor is he, within the power and scope of a Schackno proceeding. Therefore, a debtor may be compelled to deal with one class of creditors in a Schackno proceeding, and another class of creditors in another proceeding. Hence, a multiplication of suits and proceedings would depend only upon the number of the debtor's other liabilities. This multiplicity of suits is impossible in a Federal reorganization.

It is contended that a debtor, whose property is insufficient to meet the obligations of the first mortgage, being therefore bankrupt, is not to be heard to complain about a possible multiplicity of suits. But solvency is not a prerequisite in a petition for reorganization. *In re: Central Funding Corp.*, 75 Fed. (2) 256. "In all reorganizations the debtor must be insolvent in one sense or another." * * * and that accordingly a "debtor can be reorganized though its equity has lost all value." *Central Hanover* vs. *President, etc.*, 105 Fed. (2) 130. Insolvency alone is not "sufficient to prove that the petition was filed in bad faith" *Majority opinion*, R. 108-109, citing in support. *In re: Castle Beach Apartments*, 113 Fed. (2) 762 (C. C. A. 2); *In re: Julius Roehrs Co.*, 115 Fed. (2) 723 (C. C. A. 3).

The insolvency of the debtor is undoubtedly an important factor to be considered by the District Court upon the presentation of a petition. But the final consideration of the debtor's insolvency is a matter that the District Court, after its initial or preliminary determination has been made, takes up for such final determination after the debtor has proposed a plan wherein it seeks to participate. If the debtor fails to furnish additional consideration "to justify a retention of a stock interest by the present stockholders of the debtor" (*Price* v. *Spokane Silver & Lead Co.*, 97 Fed. (2d) 237, at p. 245) then the whole proceedings may be dismissed as showing a lack of good faith. But this proceeding has not reached that stage. "It is a familiar rule that the court will not anticipate the decision of a constitutional question upon a record which does not appropriately present it." *Tennessee Publishing Co.* v. *American National Bank*, 299 U. S. 18.

Thus, whether or not a debtor is solvent when it files a petition for reorganization, should not control or determine its good faith. For a debtor may acquire an interest in an insolvent estate, by making a capital contribution thereto, complying in this way, with the basic and salutary rule laid down by this Court in *Case* vs. *Los Angeles Lumber Products Co., supra.*

2. *There is no prior proceeding "pending" within the meaning of Section 146 (4) of the Bankruptcy Act.*" This is disclosed first by the wording of the order of the state court which terminated all of the prior pending proceeding therein, and second by the statutes of the State of New York.

The state court order, by its own terms, was a "final" order. It was intended to, and it actually did terminate all prior pending state-court proceedings. But the true import of this "final" order is to be derived from a reading of the New York statutes governing the procedures

whereby a new proceeding could be commenced. The Mortgage Commission Act, *supra*, was amended to provide procedural requirements whereby new proceedings could be instituted. Under Chapter 290 New York Laws 1935 (Section 1957, McKinney's Unconsolidated Laws of New York), whenever the *Mortgage Commission* (here the Schackno trustee) desires to make any proposal in exercise of any of its limited powers,

> "it shall file a copy of such proposal with the Clerk of the Court and shall prepare and mail to each holder of a mortgage investment * * * a summary of such proposal together with a notice designating a date when such court (State Court) will pass upon such proposal and hear any objection thereto on the part of any holder of a mortgage investment."

The Schackno Act, *supra*, under which the Superintendent of Insurance took possession of the defunct Bond & Mortgage Guarantee Co., was also later amended to provide similar procedural requirements whereby a *certificate holder* could initiate a new proceeding (Chap. 906 New York Laws of 1934; *Section 1801 (1-a)* of McKinney's Unconsolidated Laws of New York). The difference between these two statutes is that the first was intended to apply only to new proceedings initiated by *Schackno Trustees*, while the other governed new proceedings initiated by *certificate-holders*.

The procedural requirements of the aforesaid statutes, closely scrutinized, clearly match the jurisdictional formalities usually present when any ordinary lawsuit is commenced. The new proceeding is commenced by the filing of a petition. (In an ordinary lawsuit, this would be the summons or citation.) Thereafter, notice by mail of the filing of such petition is given to all interested parties. (This is effecting service thereof.) After such

service has been effected, objections may be interposed in opposition to the petition. (This is the equivalent of an answer.) Thereafter, and as a result of the filing of objections, controverted issues of fact may arise which the state court may be required to determine. In such a case, the state court, "if it deems it necessary, may take testimony relative thereto." (Chap. 588, New York Laws of 1935; McKinney's Unconsolidated Laws of New York, *Section 1801*, Subd. 2.)

In the light of these statutes, the meaning of the state court's "final" order takes on its true significance. It terminated all prior proceedings in the state court for good and always, and unless the procedural requirements of these statutes were complied with, no proceeding could be deemed "pending".

* * * * *

3. *In any event, the respondent had the burden of proving that they would best subserve the interests of creditors and stockholders which burden the respondent has failed to sustain.* The motion to dismiss the debtor's petition was initiated by the respondent. When the respondent's motion came on to be heard before the District Court, there already existed a determination that the debtor's petition had been filed in good faith. That was a judicial determination of law and fact, even though made *ex parte*. *In re: Cheney Bros.*, 12 Fed. Supp. 609; *O'Connor* vs. *Mills*, 99 Fed. (2) 665 (C. C. A. 8); *In re: Augustyn*, 87 Fed. (2) 577 (C. C. A. 7). Therefore, it was the affirmative duty of the respondent to prove to the satisfaction of the District Court, a contrary situation, namely, that there was a "prior pending proceeding" within the meaning of *Section* 146 (4). This burden, it is respectfully submitted, the respondent has not sustained. Indeed, we may safely say that the respondent utterly failed in this respect. For the District Court, after studying all the

evidence before it and after hearing argument pro and con, concluded that

> "Such an object (Reorganization) cannot be attained in the State Court proceeding. It may be here" (R. 72).

This finding by the District Court was based upon, not only the statutory advantages of a Chapter X reorganization, discussed in Subd. 1 hereof, but also upon the fact that the Schackno trustee, under the Declaration of Trust (R. 85-86), possesses an interest adverse to all parties concerned, including the certificate holders. The District Court, undoubtedly bearing this in mind, commented on the resulting conduct of the Schackno trustee as follows: The debtor

> "endeavored on two separate occasions to present modified plans of relief *but on each occasion has been rebuffed by the (Schackno) trustee*" (R. 73). (Italics supplied.)

This result undoubtedly arose out of the fact that the Schackno trustee herein is entitled to receive a substantial sum of money each year as compensation for its services,[2] which income would cease if the debtor's petition were approved.

> "* * * it is appropriate to observe that it (Schackno trustee) had a selfish interest not identical with the interest of the certificate holders, in having the State Court proceeding continue because the (Schackno)

[2] By contrast, the State Superintendent of Insurance never was entitled to receive any income as a result of his participation in Schackno proceedings. Such participation was deemed part of his statutory duties.

trustee derived emoluments therefrom which would terminate if the Chapter X proceeding was not dismissed" (R. 113).

A further description of Schackno trustees is to be found in the recent case of *In re: Paloma Estates*,[3] where Judge Clark, dissenting, wrote,

> "And these (the facts) show that the trustees are now acting as dogs in the manger."

It was not inappropriate to observe therefore that perhaps this selfish interest has accounted for the failure of the Schackno trustee to apprize certificate holders of its opposition to the debtors application (R. 125).

The above determination of the District Court, that reorganization could not be accomplished in the Schackno proceeding, is final unless clearly shown to be wrong. For "the question of the good faith of a debtor is one of fact, the determination of which is by statute committed to the discretion of the District Court." * * * "His finding will not be set aside unless clearly shown to be erroneous." *O'Connor* vs. *Mills*, *supra*. There must be an abuse of discretion by the District Court to justify a reversal by the Circuit Court. *In re: Augustyn*, *supra*.

Since, in the instant case, there was a failure to show such an abuse of discretion, and because reorganization under Chapter X is vastly superior to a possible reorganization under the New York Schackno Act, *supra*, the District Court was correct in dismissing the respondent's motion. It follows therefore, that it was error for the Circuit Court to reverse.

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[3] *In the Matter of Paloma Estates, Inc.* (C. C. A. 2) decided February 21, 1942, unreported as yet. Opinions printed in brief of Securities & Exchange Commission offered in support of petition for Writ of Writ of Certiorari.

POINT II.

The debtor is not personally disqualified from invoking the jurisdiction of the Federal Court under Chapter X of the Bankruptcy Act.

The reversal of the District Court by the Circuit Court was on the ground of the alleged "personal disqualification of the debtor" to invoke a proceeding under Chapter X. This holding was based upon either or both of the following reasons: 1. the debtor's participations in the State Schackno proceeding, some seven years previous to its present application, in which previous proceeding the maturity date of the debtor's mortgage was extended and its interest rate was reduced, and or 2. the reservation of jurisdiction by the State Court as set forth in the "final order" (R. 44). In either case, or both, we believe that the holding of the Circuit Court was error.

1. The nature, extent and purpose of the debtor's participation in the State Schackno proceeding in the years 1934 and 1938 are contained in the record (R. 45-51; 52-54). It is a fact that nearly every property owner, whose property was encumbered by a certificated mortgage, participated to this extent in a State Schackno proceeding. *Report to His Excellency, Herbert H. Lehman, Governor, of the State of New York, by George W. Alger*, dated October 5, 1934. This participation was inevitable because during the last decade, nearly every certificated mortgage became due, and it was necessary to treat with the owners of such mortgage in order to satisfy the mortgage, (if possible), extend their dates of maturity, reduce their rates of interest and amortization, etc. Since the owners of the mortgage, in this case, were no longer represented by the Bond & Mortgage Guarantee Co., it was necessary to deal with a representative of said Bond

& Mortgage Guarantee Co. wherever he was to be found. That representative was, by special act of the New York Legislature, (Schackno Act, *supra*) the State Superintendent of Insurance, since supplanted through various steps, by the present respondent. Thus, if the Bond & Mortgage Guarantee Co. were not rendered insolvent, the consideration of the debtor's mortgage, *i. e.*, the maturity date, interest and amortization rates, etc., could be very well taken up in its old offices. There would have been no need to go to any court. But the Bond & Mortgage Guarantee Co. did not remain solvent, so that, when the debtor's mortgage approached maturity, the debtor was compelled to follow the Bond & Mortgage Guarantee Co., into the court where its representative was to be found. Thus, it was the insolvency of the Bond & Mortgage Guarantee Co., not the insolvency of the debtor, that pulled the debtor into the State Schackno proceeding. And this would be true also for the certificate holders, who, against their will, were likewise dragged into the State Schackno proceedings. Therefore, there is no significance to be attached to fact that the debtor may have initiated a motion in the State Schackno proceeding for the purpose of satisfying, modifying or extending its mortgage. The insolvency of the Bond & Mortgage Guarantee Co. made that step a compulsory act of the debtor. For the fact is that *the debtor was not being reorganized in the state court*. Only the representative of the certificate holders was being "reorganized".

The majority of the Circuit Court holds that since "the debtor made no attempt to bring its proposals to the attention of the state court" it is not entitled to invoke federal jurisdiction (R. 110) and that its prior holding in *Brooklyn Trust Co.* vs. *Rembaugh*, 110 Fed. (2) 838 requires that it be given effect here "to prevent a debtor who has assented to a plan which is being supervised by the state court in reorganization pro-

ceedings still pending there, from flouting that jurisdiction by filing a petition in the District Court" (R. 110).

The weakness of this argument is that the debtor has no real standing in Schackno proceedings for Schackno proceedings were instituted, as we have shown, not for the benefit of the debtor who has never been in bankruptcy or reorganization in any court, but in order to rehabilitate or liquidate defunct bond and mortgage guaranty companies. *People* vs. *Title & Mortgage Guarantee Co., supra.* And that is the reason why the Schackno and Mortgage Commission Acts (*Supra*) are so significantly silent as to methods and procedure whereby a *debtor's* proposal can ever reach the state court. That also is the meaning of Judge Clark's words, in his dissent[3] "for they (Schackno Trustees) will not present the debtor's revised plan to the state court, and *that appears to be the only way it can get there*"[3] (italics supplied). Clearly, the debtor is not a real party in interest in Schackno proceedings, for its problems are of no concern to the state court and are not within its jurisdiction.

The argument, *i. e.*, that there is a "plan which is being supervised by the state court", possesses several weaknesses. First is the simple fact that there is *no* plan at the present time. Whatever plan there *was*, expired by its terms in December, 1937. There is need now for a new plan because of changed circumstances. Secondly, neither the debtor nor the plan, as such, are being supervised. There can be no misunderstanding on this score. For the state court does not now supervise the debtor or the plan. It supervises merely the enforcement of the plan by the Schackno trustee, seeing to it that its obligations to the certificate holders are faithfully discharged. *Mortgage Commission Act, supra* Section 176[7].

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[3] *In the Matter of Paloma Estates, Inc., supra.*

McKinney's Unconsolidated Laws New York. And that is because the state Schackno proceedings do not have jurisdiction over any other person or property except the indenture (Schackno) trustee, the certificate holders, and the Mortgagee. It does not have original jurisdiction over the debtor. Thus, there can be no "flouting" of the state court's jurisdiction by the debtor, as the Circuit Court has held.

The contention, that the reservation of jurisdiction by the state court, as set forth in its "final order" (p. 44) was a personal disqualification of the debtor to invoke the jurisdiction of the Federal Court, is clearly erroneous.

In the first place, the debtor never consented to this "final order". True, it was made on notice to the debtor, but its consent was never given. Therefore, there was, at most, only a technical default in making opposition to the application. And its opposition, even if it could be interposed, would have possesed no meaning or significance at that time. For the primary purpose of that "final order" was to appoint the Mortgage Corporation of New York as successor "trustee" to the Superintendent of Insurance in the administration of the defunct and insolvent guaranty company. So far as the debtor was concerned it did not matter who was the trustee of the mortgage. The purpose of serving notice on the debtor was to apprize it that, after the entry of the "final order", it was to thereafter recognize and do business with only the Mortgage Corporation of New York as successor trustee and representative of the certificate holders who had claims against the insolvent guaranty company. And since the debtor has no real standing in Schackno proceedings, the notice to the debtor could possess no legal implications, or invoke an estoppel on its part.

Secondly: the reservation of jurisdiction by the state court was over the "trust estate", not over the debtor or

its property. The "trust estate", consisted of a bond and mortgage wherein the holders of participation certificates were interested. The purpose of reserving jurisdiction over such "trust estate" was to prevent the Schackno trustee from prejudicing or compromising in any possible way the rights of certificate holders in such bond and mortgage. Thus Paragraph III of the Declaration of Trust (R. 26) provides that

> "The Trustee shall not extend any bond and mortgage, reduce the rate of interest, release any property from any mortgage except as authorized by the terms thereof or the order above referred to, nor sell the securities or the property covered thereby, *without the permission of the Court* * * *;" (Italics supplied.)

Thirdly: the open door allegedly extended to "any other interested party" in said "final order" was not intended to apply to the debtor. As we have shown, the entire proceedings were not intended to apply to the debtor. That is illustrated by the absence of a statute similar to Chapter 290, New York Laws of 1935, (*Section* 1757 of McKinney's Unconsolidated Laws of New York) and Chapter 906, New York Laws of 1934 (*Section* 1801 of McKinneys Unconsolidated Laws of New York). The first statute, Chapter 290 of New York Laws of 1935 was intended to apply to proceedings initiated by Schackno Trustee. The second statute, Chapter 906 New York Laws of 1934, was intended to apply only to proceedings initiated by certificated holders. But there is no similar section providing for a debtor's petition. On this score, the Schackno and Mortgage Commission Acts are significantly silent.

The phrase, "any other interested party" was in reality an invitation intended only for certificate holders

to come to the state court and to lay their grievances before it so that proper supervision could be had of their "trust estate". For certificate holders have had many grievances against Schackno trustees for such practices as 1. paying overriding commissions on leases, (*Matter of Bond & Mortgage Guarantee* Supreme Court, New York County, Special Term Part I, McLaughlin, J., New York Law Journal, June 28, 1941) 2. paying commissions on lease renewals, (*Matter of Lawyers Title & Guarantee Company,* (49 West 72nd Street) Supreme Court, New York County, Special Term Part I, McLaughlin, J., New York Law Journal, November 5, 1941) 3. paying premiums on agent's fidelity bonds out of the trust-estate, (*Matter of Brooklyn Trust Company,* Supreme Court, New York County, Additional Special Term, Noonan, J., New York Law Journal, April 25, 1940) 4. paying lawyers for work the trustees should do, (*In re: Lawyer's Title & Guarantee Company,* Supreme Court, New York County, Special Term Part I, McLaughlin, J., New York Law Journal, June 28, 1941) 5. paying for a servicing agent in addition to a managing agent, (*Matter of Lawyer's Mortgage Company,* (55 East 86th Street) Supreme Court, New York County, Special Term Part I, McLaughlin, J., New York Law Journal, July 9, 1941) 6. paying two sets of lawyers, (*Matter of Lawyer's Title & Guarantee Co.,* Mortgage No. 438385, Supreme Court, New York County, Special Term Part I, McLarghlin, J., New York Law Journal, June 2, 1941) and similar offenses.

Practices of these kinds were frowned upon in State Schackno proceedings. Frequently, the state courts, on their own initiative, surcharged Schackno trustees for indulging in such practices. Therefore, the invitation "to any other interested party" was extended to the certificate holders for the purpose of enlisting their aid so that the state court might be better able to protect their interests. In this way, the state court justices, who were appointed

to generally supervise Schackno proceedings, became the self-appointed watch-dogs of the interests of the certificate holders, but only as against the practices of the Schackno trustees.

In view of the foregoing, it seems clear that the debtor, having originally no standing in Schackno proceedings, is not compelled to beat down the doors of the State Court in order to gain entrance therein for a hearing on a proposed plan already rejected by a Schackno trustee possessing a selfish interest. And since, in any event, the Schackno proceeding was not instituted for the benefit of the debtor, it has an absolute right to seek admission to the only court in the land where the rights of all parties can be heard at one time.

POINT III.

The doctrine of comity has no application to this case.

It is true that the policy of the Federal Courts is not to extend their jurisdiction over matters equally cognizable by state tribunals. *Shanks* vs. *Basting Manufacturing Co.*, 9 Fed. (2) 116. But if the state tribunal is limited in jurisdiction, or its powers are limited to treat with all problems, in a given case, then the federal court's jurisdiction is exclusive to dispose of the entire cause. *Langnes* v. *Green*, 282 U. S. 531. For the rule permitting a state court to continue jurisdiction is not applicable where exclusive authority is given to the Federal Court. *In re: Prupatto*, 51 Fed. (2) 602.

Bankruptcy is an administrative feature of our law which, possessing uniform application, is a monopoly of the Federal Government. Art. 1, Section 8 (4) of the Constitution. Thus, when any state in the Union enacts an insolvency law, it is limited in application only to its

citizens. Such an insolvency law must give way to the Uniform Bankruptcy Act of Congress. For it

> "is paramount and superior to all state laws upon the subject, and all state insolvency laws are suspended insofar as they relate to the same subject-matter and affect the same persons as the National Bankruptcy Act". *First National Bank of Albuquerque* vs. *Robinson*, 107 Fed. (2) 50, at p. 53.

Even more is it necessary to suspend the operation of a state insolvency law (here the Schackno Act) when it appears that it was not intended to apply to the debtor, or that it was a special type of proceeding applying only to certain interested parties.

Thus, let us assume, arguendo, that in 1934 the debtor had several other classes of creditors.[4] Does it follow that because the debtor and one class of creditors involved themselves in 1934 in that special type of proceeding that the debtor is thereafter to be barred from taking all of its creditors, of every class and description, into the Federal court where all and every of its problems can be considered at one time? To do so would result in judicially enlarging the jurisdiction of that special type of proceeding beyond the limits of the statute which created it. It would also be in direct violation of the rule of law laid down by this court in the case of *John Hancock Mutual Life Insurance Co.* vs. *Bartels*, 308 U. S. 180, where the court held that a debtor should not be charged with bad faith merely because he takes a course provided for him by Congress, Chief Justice Hughes, writing the opinion of the court said:

> "the plain purpose of Section 75 was to afford relief to debtors who found themselves in economic distress

[4] The debtor did then have (R. 79) and even now has several types of creditors (R. 70; 71, 91, 92, 93).

> however severe, by giving them the chance to seek an agreement with their creditors. Subsection (a) to (r) and, failing this, to ask for the other relief afforded by subsection (s)".

Even the Circuit Court of Appeals for the Second Circuit, in the case of *In re: Koch*, 116 Fed. (2) 243, recognized that a

> "debtor has a legal right to have her property administered in bankruptcy".

Since, as we have shown, Schackno proceedings are limited in nature, jurisdiction and safety, and are intended to apply only to a certain special group of creditors, it follows that its operation should be suspended when the Federal Bankruptcy Act is properly invoked.

POINT IV.

Regardless of the personal disqualification of the debtor, it was error to dismiss its petition for reorganization in the interest of creditors.

As shown, a reorganization proceeding under Chapter X possesses many inherent advantages over a possible reorganization under the New York State Schackno Act. Those advantages, so far as the creditors are concerned, would be denied to them merely because it was not they who had invoked their application. This kind of reasoning, we submit, does violence to one of the main purposes of the Bankruptcy Act, *i. e.*, protection of creditor's rights.

Concededly, the interests of creditors are paramount to the interests of stockholders. Why therefore, should their best interests be overlooked, and in this case, re-

jected, because of some alleged personal disqualification on the part of the debtor, a disqualification which in reality does not exist, or if existing is purely technical? Yet that is the holding of the Circuit Court which, we submit, is "basic error". *Opinion of Judge Frank* (R. 116).

The Circuit Court dismissed the debtor's petition on the theory of an election of remedies, and that the debtor, having already made its election, could not now be heard to complain. But, as Judge Frank wrote in his dissent,

> "that harsh doctrine is fast becoming weaker even in its traditional strongholds and I cannot acquiesce in an attempt to import it into the streamlined procedure of the Chandler Act. A Chapter X procedure is not a piece of litigation in which the debtor is one of the contending parties, a lawsuit in which it seeks relief against someone else" (R. 125).

and further

> "Even if the doctrine were applicable I cannot understand why any such election of remedies by the debtor should be determinative of what is for the best interests of the creditors. Again, viewing the situation realistically, it is obvious that the certificate holders themselves have not, in any real sense, elected in favor of the state court proceeding" (R. 125).

As shown, neither the debtor, nor the certificate holders ever elected in favor of the state court proceedings. The creditors, like the debtor, were dragged into it, not of their own choice, but because of the insolvency of the Bond & Mortgage Company. To therefore deny certificate holders the benefits of the National Bankruptcy Act, merely because they did not possess the initiative to

invoke it, is a holding which ignores the historical facts of the last decade.

> "Anyone familiar with the realities of corporate reorganizations * * * knows that scattered individual security holders, such as the individual certificate holders in this case, are not at all informed as to their rights", * * * and "ignorant of their theoretical rights, as most such security holders are, they seldom exercise them, but, instead, usually go along with whatever proceedings have already been instituted" * * * Indeed, it was the "well-known inertia of such security holders which led to the enactment of many of the provisions of Chapter X" *Opinion of Judge Frank* (R. 120).

And this court has held in the recent case of *Securities & Exchange Commission* vs. *U. S. Realty & Improvement Co.*, 310 U. S. 434, that one of the principal purposes of a proceeding under Chapter X was to provide "detailed safeguards designed to protect the interests of public investors".

The Circuit Court, however, because of an alleged disqualification on the part of the debtor, would defeat the best interests of the creditors. This would be in direct violation of the firmly established rule of law "that the real purpose and intent of the legislative body must prevail over the literal import of the words used". *Securities & Exchange Commission* v. *U. S. Realty, supra.* It would thus produce a result which Judge Clark, in his *Paloma* dissent, *supra*, describes as follows:

> "I cannot avoid the conviction that we are substituting an inadequate state proceeding for the carefully safeguarded proceedings in reorganization devised by Congress for cases such as this, where the public interest may be protected by the public agency of the Securities & Exchange Commission".

Judge Frank, in his dissent in the court below, said that

> "even if it could be said that the certificate holders had acquiesced in the prior proceedings, nevertheless, no theory of election or estoppel should control since, under clause (4) the inquiry must be what is for their best interests" (R. 125-126).

Therefore,

> "the more the bad faith of the debtor and those confederating with it in such circumstances, the more reason the bankruptcy courts should take jurisdiction. * * * The interests of the security holders in a successful and needed rehabilitation should be deemed superior to the possibly questionable motives of the debtor" (R. 124).

Since, in this case, there is no suggestion of or justification for ascribing sinister or unfair motives on the part of the debtor in filing its petition, the error in the holding of the Circuit Court becomes a grevious one, which in the interests of the creditors alone, requires a reversal.

CONCLUSION.

The order of the Circuit Court should be reversed and order of the District Court affirmed.

Respectfully submitted,

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FILE COPY

Supreme Court, U. S.
FILED
MAR 4 1942
CHARLES ELMORE CROPLEY

No. ~~948~~ 24

In the Supreme Court of the United States

OCTOBER TERM, 1941

MARINE HARBOR PROPERTIES, INC., PETITIONER

v.

MANUFACTURERS TRUST COMPANY, AS TRUSTEE; MAURICE RUBINGER, TRUSTEE OF MARINE HARBOR PROPERTIES, INC., ET AL.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM FOR THE SECURITIES AND EXCHANGE COMMISSION

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ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM FOR THE SECURITIES AND EXCHANGE COMMISSION

The Securities and Exchange Commission became a party in the District Court to the present proceeding for the reorganization of Marine Harbor Properties, Inc., under Chapter X of the Bankruptcy Act.[1] The Commission also participated as an appellee in the proceedings before the Circuit Court of Appeals, and the petition for a writ of

[1] The Commission became a party pursuant to the provisions of Section 208 of the Bankruptcy Act (11 U. S. C., Sec. 608).

certiorari filed by the Debtor names the Commission as a respondent.

The Commission is in doubt, however, whether it should properly be regarded as a respondent before this Court, since it has consistently supported the position taken by the petitioner and must therefore be considered as aligned in interest with the petitioner. If the Commission is properly to be considered as a respondent, we ask the Court to regard this memorandum as a memorandum for the respondent Commission joining in the petition for certiorari. If the Commission is not properly to be regarded as a respondent, we ask the Court to regard this memorandum as a memorandum for the Commission, as *amicus curiae*, in support of the petition.[2]

OPINIONS BELOW

The opinions of the Circuit Court of Appeals (R. 107–126) are not yet reported. The opinion of the District Court (R. 70–75) is reported in 41 F. Supp. 814.

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[2] The Commission is not filing a separate petition for certiorari because that would raise an issue as to whether the Commission, which under Section 208 of the Bankruptcy Act may not take an appeal to the circuit courts of appeals, may nevertheless file a petition for a writ of certiorari to review an adverse decision of a circuit court of appeals in a case where the Commission was an appellee in the circuit court of appeals. It seems preferable that the clear-cut issue in the present case not be confused by this extraneous issue.

JURISDICTION

The decree of the Circuit Court of Appeals was entered on January 27, 1942 (R. 126). The petition for a writ of certiorari was filed on February 13, 1942. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Section 141 of the Bankruptcy Act provides that a petition filed by a debtor under Chapter X shall be dismissed if not filed in good faith, and Section 146 (4) provides that a petition shall be deemed not to be filed in good faith if "a prior proceeding is pending in any court and it appears that the interests of creditors and stockholders would be best subserved in such prior proceeding." The question presented is whether, under these provisions, a bankruptcy court must relinquish the jurisdiction conferred upon it by Chapter X in favor of a pending state court reorganization proceeding upon a mere showing that the debtor company, which filed the petition under Chapter X, once consented to a plan in the state court proceedings for an extension of a mortgage on its property, and without any showing that the interests of the debtor's creditors and stockholders would be better safeguarded in the state court proceeding than in proceedings under Chapter X.

STATUTE INVOLVED

Section 141 of the Bankruptcy Act (11 U. S. C., Sec. 541) provides as follows:

> Upon the filing of a petition by a debtor, the judge shall enter an order approving the petition, if satisfied that it complies with the requirements of this chapter and has been filed in good faith, or dismissing it if not so satisfied.

Section 146 of the Bankruptcy Act (11 U. S. C., Sec. 546) provides in part as follows:

> Without limiting the generality of the meaning of the term "good faith," a petition shall be deemed not to be filed in good faith if—* * * (4) a prior proceeding is pending in any court and it appears that the interests of creditors and stockholders would be best subserved in such prior proceeding.

STATEMENT

The relevant facts are set forth in the Debtor's petition (pp. 4–6) and need not be repeated here.

ARGUMENT

1. In Chapter X of the Bankruptcy Act, the Congress exercised its paramount bankruptcy power to provide a procedure for the reorganization of distressed corporations. However, in order to assure that this procedure would not be used to defeat rather than to accomplish the congressional objective of protecting security holders, Congress provided in Section 141 that the Dis-

trict Courts are not to assume jurisdiction of a debtor's petition under Chapter X if it is not filed in good faith, and in Section 146 (4) that a petition shall be deemed not to be filed in good faith where a prior proceeding is pending in another court "and it appears that the interests of the creditors and stockholders would be best subserved in such prior proceedings."

In the present case, and in other similar cases as well,[3] the court below ruled that these provisions of the Act require the district courts to dismiss all petitions filed by a debtor company whenever it is shown that the debtor actively participated in prior state court proceedings, irrespective of whether the prior proceedings provide safeguards for public investors comparable to those found in Chapter X. This construction of the Act, with its emphasis upon an assumed personal disqualification on the part of the debtor and its disregard of the interests of the debtor's creditors and stockholders, is, we believe, contrary to both the clear terms and the obvious purpose of the statute; even more important, it serves to deprive the security holders of a large

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[3] *Brooklyn Trust Co.* v. *Rembaugh*, 110 F. (2d) 838; *In re Paloma Estates, Inc.*, decided February 21, 1942, after the petition in this case was filed. Judge Clark, dissenting in the *Paloma* case, referred with approval to the dissent of Judge Frank in the present case. For the convenience of the Court the opinions in the *Paloma* case are printed in the Appendix, *infra*, pp. 15–23.

and important class of corporations of the protection which Congress quite evidently intended to confer upon them by the enactment of Chapter X. Accordingly, the decision seems plainly to call for review by this Court.

2. The Court has recently had occasion to examine the entire structure of Chapter X. *Securities and Exchange Commission* v. *U. S. Realty & Improvement Co.*, 310 U. S. 434. As was there observed, Chapter X provides an integrated and carefully fashioned procedure for the reorganization of corporations and for the protection of their security holders. Provision is made, *inter alia*, for "control by the court over security holders' committees and the formulation of reorganization plans" (310 U. S. 449); for securing "impartial and expert administrative assistance" through participation in the proceedings by the Securities and Exchange Commission (*ibid.*); for the appointment of a disinterested trustee and for an investigation and report by such trustee concerning the debtor's financial problems and management; and for assuring that security holders will not be required to vote on any proposed plan of reorganization until they have received full information concerning the plan and until the plan has been initially approved by the court.

This procedure, as Section 256 of Chapter X makes clear, is to supersede all conflicting state procedures except, as stated in Section 146 (4), where a prior state court proceeding is pending and

the interests of creditors and stockholders would be best subserved in such prior proceedings. The mere pendency of prior state court proceedings is immaterial; they must be of such character or have proceeded to such a point that the security holders would be harmed rather than helped by calling the remedial provisions of Chapter X into play.

The court below disregarded this statutory standard. It undertook to direct dismissal of the petition, not because of the character of the prior state court proceeding, but because of an asserted "lack of good faith flowing from the personal disqualification of the debtor" (R. 111). It is not clear whether this result was thought to follow from the general provision of Section 141, requiring dismissal of all debtors' petitions not filed in good faith, or from the specific provision of Section 146 (4), requiring the dismissal of a debtor's petition where a prior proceeding is pending in which the interests of the security holders would be better subserved than under Chapter X. The court said that there was no "absence of good faith * * * in the broad meaning of those words," and yet, in the next sentence, stated that the special circumstances set forth in Section 146 (4) are "not to be confused with what controls here" (R. 111). Whichever provision the court may have thought applicable, however, we believe its decision to be clearly erroneous.

3. The alleged "personal disqualification of the debtor," the court said, arose because the Debtor

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had once consented to an extension of the mortgage on its properties approved by the state court and had failed to apply to the state court for further relief after the extension expired. Whether the Debtor had the power itself to present an application to the state court for further relief is a question on which the majority of the court below and the District Judge were in disagreement (see R. 110, 71–72, 74–75; see also dissenting opinion of Judge Clark in the *Paloma* case, Appendix, *infra*, p. 22). But whether or not the Debtor might have had recourse to the state court, its failure to do so and the exercise of its statutory right to file a petition under the Bankruptcy Act do not constitute bad faith. As this Court has held in a proceeding under Section 75 (s) of the Bankruptcy Act, a debtor should not be charged with bad faith because he takes the course provided for him by Congress. *John Hancock Mutual Life Insurance Co.* v. *Bartels*, 308 U. S. 180, 185. And, as the court below held in a case involving Chapter XI of the Bankruptcy Act, in answer to the contention that the proceeding had been filed to avoid a state fraud receivership, "the answer is that the debtor has a legal right to have her property administered in bankruptcy." *In re Koch*, 116 F. (2d) 243, 247.

Moreover, the assumption that the personal bad faith of the debtor, if deemed to exist, is relevant to the propriety of the exercise of juris-

diction by the bankruptcy court ignores the essential elements of the statutory scheme devised by Congress. Congress provided the safeguards of Chapter X for the benefit of *investors*; it directed that consideration be given to the interests of *creditors* and *stockholders*. To ignore the real parties in interest and to attach weight to the conduct of the fictional legal entity known as the debtor is to nullify the purposes of the Act. The motives of the debtor itself are unimportant, because once the petition is filed the court, not the debtor, has control of the proceedings. See *Case* v. *Los Angeles Lumber Products Co. Ltd.*, 308 U. S. 106, 125–126. Under the rule enunciated in that case the debtor and its stockholders can gain no strategic advantage from the pendency of the proceedings and their interests will be entirely eliminated unless a surplus remains after payment of all creditors in full (*id.*, 131). Indeed, the more questionable may be the motives of the debtor or the persons controlling it, the more reason there is for the court to take jurisdiction and to make available to creditors and stockholders the safeguards of Chapter X.

4. Had the court below directed its attention, not to the alleged "personal disqualification" of the debtor, but to the effect of the dismissal of the petition upon the interests of the creditors and stockholders, its decision would necessarily have been different.

The prior proceeding has been conducted under the so-called Schackno and Mortgage Commission Acts of New York,[4] which lack almost all the basic safeguards for the protection of securityholders provided by Congress in Chapter X. There is no searching investigation of the debtor's past management and of its present business and prospects which is required through the medium of an independent trustee under Section 167 of the Bankruptcy Act. There is no provision similar to that requiring participation in Chapter X reorganization proceeding by the Securities and Exchange Commission.[5] There is no requirement that a plan must receive preliminary approval by the court before the assent of securityholders may be obtained (cf. Section 176 of the Bankruptcy Act) or that information must be furnished to securityholders (cf. Section 175 of the Bankruptcy Act); and there are no protective provisions as to the form of reorganization (cf. Section 216 of the

[4] L. 1933, c. 745 as amended, N. Y. Unconsolidated Laws, § 1796 *et seq.*; L. 1935, c. 19 as amended, N. Y. Unconsolidated Laws, § 1751 *et seq.*

[5] It is true that the court having jurisdiction of the state court proceedings in the county in which the state court proceedings in this case are pending has established an organization known as the Bureau of Trust Supervision. There is nothing to show, however, that this Bureau has facilities similar to those of the Securities and Exchange Commission for providing advice to the court or a record of achievement in that field.

Bankruptcy Act). Indeed, Chapter X has the same superiorities over the state court procedure as this Court held that it has over the procedure provided in Chapter XI of the Bankruptcy Act. See *Securities and Exchange Commission* v. *U. S. Realty & Improvement Co., supra.*[6]

Nor can there be any contention that the particular proceeding here involved had proceeded to such a point that the maintenance of the Chapter X petition would have been adverse to the interests of investors. To be sure, a "plan" had been approved by the state court in December 1934, but this "plan" merely provided for an extension of the mortgage and the extension expired in 1937 (R. 52, 45). A modification of the plan was approved in 1938; this modification, however, merely established a trustee to act for security holders, without effecting any adjustments of the rights of the certificate holders *vis a vis* the Debtor (R. 38, 22). In the modified plan the state court retained jurisdiction to consider further applications for relief (R. 44), but no such applications were filed.[7] Negotiations between the trustee and the Debtor were un-

[6] See Note (1934) 34 Col. L. Rev. 663; Note (1935) 35 Col. L. Rev. 874; Note (1941) 18 N. Y. U. L. Q. Rev. 399, 418; Siegel, *Chapter X or Schackno Act Proceedings?* (1941) 27 Corn. L. Q. 56.

[7] The Debtor clearly assumed that the reservation of jurisdiction did not empower it to make such an application (R. 62, 67–68).

dertaken but proved futile (R. 14). Thereafter the Debtor defaulted in the payment of interest due April 1, 1941 (R. 12). Since the Schackno Act proceeding gave the creditors no remedy for such default, foreclosure proceedings were commenced and a receiver was appointed to take possession of the Debtor's properties (R. 12–13). Subsequently, negotiations for further extension and modification of the mortgage were undertaken, but they again proved unsuccessful (R. 14). The proceedings having reached this point, unless liquidation through foreclosure sale to an outsider occurs, a new plan must be adopted. No such plan had been promulgated in the foreclosure proceeding at the time the petition under Chapter X was filed.

It seems evident, therefore, that neither the provisions of the statute pursuant to which the state court proceedings were brought, nor the actual history of those proceedings, furnishes any ground for holding the interests of creditors and stockholders would be best served by the dismissal of the Chapter X proceeding.

5. The importance of the issue involved in this case is manifest. Thousands of certificated mortgage issues are being "reorganized" in the state courts, and many of these "reorganizations" have taken the form, as in the present case, of a short extension of the maturity of the mortgage. As

these extensions expire, further "reorganization" is needed. The decision in the present case will, to a large extent, determine whether the federal procedure provided by Chapter X shall be available for such further reorganization.

It is no answer to say that the court below only held the Debtor disqualified to file a petition under Chapter X and that, despite this decision, the federal remedy may be invoked by a petition filed by three security holders having claims aggregating at least $5,000. As Judge Frank pointed out in his dissenting opinion, such security holders are generally ignorant of their theoretical rights and consequently "seldom exercise them, but, instead, usually go along with whatever proceedings have already been instituted" (R. 120). Indeed, as Judge Frank further pointed out (*id.*), it was precisely such inertia on the part of security holders which led to the enactment of many of the provisions of Chapter X.[8]

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[8] The fact that resort has been had to the federal procedure in only a few cases thus far does not indicate that the persons concerned do not choose to resort to it. It would seem rather to indicate that the line of decisions in the Circuit Court of Appeals for the Second Circuit, begun in *Brooklyn Trust Co.* v. *Rembaugh*, 110 F. (2d) 838, and *In re Blinrig Realty Corp.*, 114 F. (2d) 100 (both decided early in 1940), and continued in the present case, and *In re Paloma Estates, Inc.* (*infra*, pp. 15–23), has discouraged any extensive resort to Chapter X.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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MARCH 1942.

APPENDIX

UNITED STATES CIRCUIT COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 152—October Term, 1941.

(Argued January 8, 1942. Decided February 21, 1942.)

In the Matter
—of—
PALOMA ESTATES, INC.,
Debtor-Appellant.

SERIES C-2 TRUSTEES AND SECURITIES AND EXCHANGE COMMISSION,
Appellees.

CHASE, *Circuit Judge:*

The debtor, which owns, subject to a first and to a second mortgage, an apartment house and lot at 200 West 86th Street in the City of New York, filed its petition for reorganization in the District Court for the Southern District of New York under Chapter X of the Bankruptcy Act. The

judge, holding that the petition was not filed in good faith within § 146 (4) of Chapter X, and also that the debtor had not complied with the general good-faith requirement of our decisions in *Brooklyn Trust Company* v. *Rembaugh*, 110 F. (2) 838, and *In re Blinrig Corp.*, 114 F. (2) 100, dismissed the petition. The debtor has appealed and is supported by the Securities and Exchange Commission, which, at the request of the judge, filed its notice of appearance and became an intervening party to the proceedings as provided by § 208 of the Bankruptcy Act. It has filed a brief in this court and has been heard on the oral argument. Other parties are permanent trustees appointed by the state court, for holders of certificates under the first mortgage and who have appeared to contest this appeal; the second mortgagee and some unsecured creditors.

The debtor is insolvent and its serious financial difficulties are of some years' standing. The first mortgage on the apartment house to which it holds title is for $2,650,000.00 and is of the kind known as a certificated mortgage which was guaranteed as to the payment of principal and interest by the New York Title and Mortgage Company. The certificates are part of such securities to the amount of $24,000,000.00 held by the above-mentioned permanent trustees who are otherwise known as the Series C–2 Trustees. The second mortgage is for the face amount of $300,000.00 and there is admittedly due on it $60,000.00 or $65,000.00. The unsecured indebtedness is approximately $3,000.00. The apartment house is assessed for taxation by the City of New York at

$2,630,000.00 and has a gross rent roll of $360,000.00 per year. The net rent income does not appear.

In August 1933, the Superintendent of Insurance of the State of New York, took possession, as rehabilitator, of the assets and business of the New York Title and Mortgage Company. Following that, the Mortgage Commission of the State of New York, as successor to the Superintendent, proposed a plan under the Schackno Act (Chap. 745 of the New York Laws of 1933, as amended), and the Mortgage Commission Act (Chap. 19 of the New York Laws of 1935) for the appointment of permanent trustees for the Series C-2 issue. This plan was approved by the state court on Jan. 15, 1936, and on April 6, in the same year, the court appointed Messrs. Frank L. Weil, William E. Russell and Raymond J. Scully such trustees. They have since been acting as such and are the appellees here.

Among the assets which came into their possession were the bond and mortgage of the debtor which have previously been referred to as the first mortgage on the apartment house. There were arrears of $255,990.00 in interest and of $212,000.00 in principal. The debtor proposed to the trustees that the amount of the interest payments overdue be compromised; future amortization of the principal sum and the payment of the part in arrears be waived; the maturity date of the mortgage extended; and the interest rate reduced. The trustees approved and applied to the state court for permission to accept the debtor's offer. That permission was granted on Aug. 7,

1936 and an extension agreement pursuant to the proposal was entered into. The maturity date of the mortgage was thereby extended to July 31, 1941 upon condition that the debtor pay interest at the rate of 4½% for two years beginning Aug. 1, 1936; at the rate of 4¾% for two years thereafter; and at the rate of 5% for the balance of the term.

The debtor made the payments as agreed with the exception of the taxes due April 1, 1940 and the interest due May 1, 1940 and later cured both those defaults. Before any default, the debtor had had some negotiations with the trustees in respect to a modification of the extension agreement which finally took the form of an offer by the debtor to buy the mortgage for $1,700,000.00 payable within ninety days partly in cash and the remainder in Series C-2 certificates. The trustees sought leave of the state court to accept this offer and it was granted on July 16, 1940. The debtor then presented evidence that the mortgaged property was worth only $1,700,000.00 and it is evident that this valuation was accepted as fair and reasonable. The offer was duly accepted but the debtor did not perform. On Oct. 1, 1940 it defaulted in the payment of taxes then due. On Nov. 1, 1940 it defaulted in the payment of interest and then notified the trustees that it was unable to purchase the mortgage as agreed. The debtor then assigned the rents to the trustees and they appointed its president agent to manage the property. Following that the debtor made another offer to buy the mortgage and informal conferences were had with the judge in charge of the proceedings in the state

court in respect to it. It was not altogether satisfactory to the trustees and before any formal action was taken on it the judge died. The debtor urged the trustees to present the matter for approval to the successor judge who declined to consider it otherwise but the trustees were unwilling to accept the offer and so took no steps to obtain leave to do so.

After the rents were assigned to the trustees and the president of the debtor acted as managing agent of the property the carrying charges were not earned and the amount in arrears when the rents were assigned had been increased during the period from Nov. 1, 1940 to May 31, 1941 to the extent of $5,902.80 making them as of June 1, 1941 $86,724.80.

With affairs in that situation the trustees removed the managing agent as of June 16, 1941 and notified the debtor of their intention to foreclose the mortgage in the state court. There has apparently been no accounting by the managing agent for the period he acted as such in June. Following the removal of the managing agent the petition for reorganization was filed in the district court.

The trustees moved to dismiss the petition as not filed in good faith for several reasons upon which they still rely. One of them was and is that "the prior proceedings in the Supreme Court of the State of New York will best subserve the interests of creditors and stockholders." The district judge after consideration reached that conclusion. This was beyond question an ade-

quate legal ground for the dismissal for lack of filing in good faith under § 141 since it falls precisely within § 146 (4) of the Bankruptcy Act and if the proof warranted the conclusion it will be unnecessary to consider any other ground for dismissal.

We think the facts well support the judge's conclusion. Though there might be a reorganization under Chap. X of the Bankruptcy Act, the value of the debtor's property is so small compared to the amount due on the first mortgage that under *Case* v. *Los Angeles Lumber Products Co. Ltd.*, 308 U. S. 106, only the certificate holders represented by the appellee trustees could have any equity to be preserved. See also, *Consolidated Rock Products Company* v. *Dubois*, 312 U. S. 510. There is nothing to indicate that their interests would, or could, be better protected in the district court. There would be increased expense and delay without any compensating advantages. And it would be inequitable to subject the certificate holders to such expense in time and money when their security, already inadequate, is being well applied to subserve their best interests in the prior state court proceedings. See, *Chapman Bros. Co.* v. *Security-First National Bank*, 111 F. (2) 86. At least, the district judge so decided and that determination is final unless clearly shown to be wrong. *Tennessee Publishing Co.* v. *American National Bank*, 299 U. S. 18; *Wayne United Gas Co.* v. *Owens-Illinois Glass Co.*, 91 F. (2) 827.

Affirmed.

CLARK, *Circuit Judge* (dissenting):

Prior to this case I had been called on but once to participate in the conflict which appears to have developed in this Court between bankruptcy reorganization and state Schackno Act proceedings with regard to concerns engaged in the certificated mortgage business in New York. *In re Blinrig Realty Corp., supra.* There I overcame my doubts as to our emerging law because of the weakness on the facts of the case presented; indeed, we were told in argument that the district court had already dismissed the petition, notwithstanding its original approval. Now we come to another case which I find far from reassuring; and I may say the same as to *In the Matter of Marine Harbor Properties, Inc.*, 2 Cir., —— F. 2d ——. Compare Judge Frank's powerful dissent in the latter case, as well as Judge Bright's decision, D. C. S. D. N. Y., 41 F. Supp. 814, which was reversed; also the law-review criticisms, Siegel, *Chapter X or Schackno Act Proceedings*, 20 Corn. L. Q. 56–73; 18 N. Y. U. L. Q. Rev. 399, 418. I cannot avoid the conviction that we are substituting an inadequate state proceeding for the carefully safeguarded proceedings in reorganization devised by Congress for cases such as this, where the public interest may be protected by the public agency of the Securities and Exchange Commission. And this, it seems to me, is as practically undesirable as it is legally unjustified.

Here we have strikingly illustrated the difficulties of our present approach. Perhaps foreclosure is the best way for all, but we have no real evidence on the point save for the affidavits

of the appearing parties. And these show that the trustees are now acting as dogs in the manger; for they will not present the debtor's revised plan to the state court, and that appears to be the only way it can get there. Though we cannot be sure without testimony, we can conclude that in the present state of the real-estate market, a sale, even at a reduced price, might easily prove to the best interests of all, including the certificate holders. In other words, the matter ought to be before a court for decision, not left solely to the not wholly disinterested trustees.

The stress placed here upon the district judge's finding seems to me not to dispose of the problem. He made no investigation; he had before him only the affidavits now before us. And his finding is most general, merely that the trustees' defenses, formally pleaded, "are sufficient in law and sustained by the proof." Moreover, his opinion shows that he relied on our previous decisions, and was unduly concerned—as I believe we have been—in the activities of the debtor and how it may have estopped itself. This, I believe, was the initial error in *Brooklyn Trust Co.* v. *Rembaugh, supra,* since repeated in the other decisions. For the statute here pertinent, authorizing dismissal of the reorganization petition when it appears "that the interests of creditors and stockholders would be best subserved" in the prior state proceeding, Bankruptcy Act, § 146 (4), 11 U. S. C. A. § 546 (4), requires a definite finding as to the interests of *creditors and stockholders,* not of the debtor. I think we should limit our former precedents to make it clear that the judge must con-

duct the investigation thus so clearly required (wherein, too, the assistance of the Securities and Exchange Commission could be sought and might well prove invaluable), and that we should take the first step thereto in a case such as this, where the facts already disclosed seem to call so clearly for a more searching inquiry. I would reverse for a hearing on the facts.

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No. 24

In the Supreme Court of the United States

OCTOBER TERM, 1942

MARINE HARBOR PROPERTIES, INC., PETITIONER

v.

MANUFACTURERS TRUST COMPANY, AS TRUSTEE; MAURICE RUBLINGER, TRUSTEE OF MARINE HARBOR PROPERTIES, INC., ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION

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ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION

The Securities and Exchange Commission became a party to the present proceeding for the reorganization of Marine Harbor Properties, Inc., under Chapter X of the Bankruptcy Act,[1] participated as an appellee before the Circuit Court of Appeals, and is named respondent herein.

This brief for the Commission is in support of the petitioner.

[1] The Commission became a party pursuant to the provisions of Section 208 of the Bankruptcy Act (11 U. S. C., Sec. 608).

OPINIONS BELOW

The opinion of the District Court (R. 70–75) is reported in 41 F. Supp. 814. The opinions of the Circuit Court of Appeals (R. 107–126) are reported in 125 F. (2d) 296.

JURISDICTION

The decree of the Circuit Court of Appeals was entered on January 27, 1942 (R. 126). The petition for a writ of certiorari was filed February 13, 1942, and granted March 16, 1942. The jurisdiction of this Court rests upon Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Section 141 of the Bankruptcy Act provides that a petition filed by a debtor under Chapter X shall be dismissed if not filed in good faith. Section 146 provides that, without limiting the generality of the term "good faith," a petition shall be deemed not to be filed in good faith if "(4) a prior proceeding is pending in any court and it appears that the interests of creditors and stockholders would be best subserved in such prior proceeding." The question presented is whether, under these provisions, a bankruptcy court must relinquish the jurisdiction conferred upon it by Chapter X upon a mere showing that

a state court has continuing jurisdiction over the trust which holds the mortgage on the debtor's property and that the petitioning debtor company once consented to an extension of the mortgage in the state court proceedings, and without any showing that the interests of the debtor's creditors and stockholders would there be better safeguarded than in proceedings under Chapter X.

STATUTE INVOLVED

Section 141 of the Bankruptcy Act of July 1, 1898, c. 541, 30 Stat. 544, as amended (11 U. S. C., Sec. 541) provides as follows:

> Upon the filing of a petition by a debtor, the judge shall enter an order approving the petition, if satisfied that it complies with the requirements of this chapter and has been filed in good faith, or dismissing it if not so satisfied.

Section 146 of the Bankruptcy Act of July 1, 1898, c. 541, 30 Stat. 544, as amended (11 U. S. C., Sec. 546) provides in part as follows:

> Without limiting the generality of the meaning of the term "good faith", a petition shall be deemed not to be filed in good faith if— * * *. (4) a prior proceeding is pending in any court and it appears that the interests of creditors and stockholders would be best subserved in such prior proceeding.

STATEMENT[2]

The Debtor's principal asset is an apartment building in New York City, which is subject to a first mortgage of $370,000 (R. 76). This mortgage is held by the respondent, Manufacturers Trust Company (successor by merger to The Mortgage Corporation of New York), as trustee for approximately 90 certificate holders. There are also junior mortgages (R. 79). On the basis of an affidavit concerning its value (R. 56), the property appears to be worth less than the amount of the first-mortgage debt (R. 71).

When originally created in 1931, the first mortgage was held by Title Guarantee & Trust Company, which issued and sold to the public certificates of participation therein, guaranteed as to principal and interest by Bond and Mortgage Guarantee Company (R. 8). In 1933, nearly all mortgage guarantee companies in New York State

[2] Because this case has been characterized by respondent mortgage trustee's attorney, in a letter dated March 28, 1942, to the Clerk of this Court, as being "generally regarded as involving a test as to whether approximately $700,000,000 in principal amount of certificated mortgages covering real estate in New York City and immediately adjoining counties will be reorganized under a procedure established by the New York Legislature or pursuant to the procedure provided in Chapter X of the National Bankruptcy Act," the statement of the case here presented has been broadened to make clear the nature of the procedures established by the New York Legislature and to show that these procedures are involved in the present case only to a limited extent.

including Bond and Mortgage Guarantee Company, were in financial difficulties as a consequence of the impact of the depression upon real estate and the resulting widespread defaults in the payment of interest, taxes, and principal.[3] It therefore became necessary for the Superintendent of Insurance to take over the mortgage guarantee companies for rehabilitation or liquidation pursuant to Article XI of the New York Insurance Law;[4] in the case of Bond and Mortgage Company, the Superintendent of Insurance took possession of its property and business in August 1933 (R. 8–9).

In the course of his efforts to rehabilitate the mortgage guarantee companies, the Superintendent had necessarily to consider problems involving the rights of the certificate holders in the mortgages which secured their investments. Emergency legislation was deemed essential to meet the special problems of this aspect of the mortgage guarantee situation.[5] The need was partially met by the Schackno Act[6] which con-

[3] Report of George W. Alger, Commissioner of His Excellency Herbert H. Lehman, Governor of the State of New York, dated October 5, 1934 (herein referred to as the Alger Report), at p. 3.

[4] Alger Report, p. 5.

[5] Annual Report of the Mortgage Commission of the State of New York, 22 N. Y. Leg. Doc. (1939) No. 94 (herein referred to as Final Report, Mortgage Commission), p. 3.

[6] N. Y. Laws 1933, c. 745 as amended; N. Y. Unconsolidated Laws, Secs. 1796 *et seq.*

ferred additional powers on the Superintendent of Insurance and established a statutory state court procedure applicable to certificated mortgage issues. This legislation was supplemented in 1935 when the Legislature adopted the Mortgage Commission Act,[7] which provided an alternative state court procedure, and which created the Mortgage Commission of the State of New York as an independent statutory representative of the certificate holders and as administrator of the certificated bonds and mortgages. The Superintendent of Insurance retained his functions as rehabilitator of the guarantee companies.

These emergency statutes recited as their purpose the protection of the guarantee companies against claims on the guarantees arising from defaults on the underlying mortgages.[8] To that end they provided statutory procedures to prevent or cure defaults by (1) adjusting the legal relations of the certificate holders so that effective action could be taken in their behalf without the necessity of obtaining their unanimous consent; and (2) creating powers for modifying the certificated mortgages so that the security for the certificate holders' claims could for the time being be adequately preserved.[9] The procedure finally evolved accom-

[7] N. Y. Laws 1935, c. 19 as amended; N. Y. Unconsolidated Laws, Secs. 1751 *et seq.*

[8] Schackno Act [L. 1933, c. 745, as amended], Section 1; Mortgage Commission Act [L. 1935, c. 19, as amended], Section 1.

[9] Final Report, Mortgage Commission, at p. 4.

plished the first of these purposes by concentrating the powers of certificate holders in individual trustees who would take possession of the certificated bonds and mortgages from the Mortgage Commission and who would, pursuant to declarations of trust, administer them as trust estates on behalf of certificate holders. Effective servicing of the mortgages pending the appointment of such trustees was facilitated by empowering the Superintendent of Insurance, and later the Mortgage Commission, to promulgate proposals for the extension and modification of the mortgages which could be made binding upon all certificate holders upon the acquiescence of two-thirds indicated affirmatively or by failure to dissent.

In the instant case, these statutes were utilized fully. First, the Superintendent of Insurance sought to preserve the certificated mortgage by promulgating, pursuant to the powers granted by the Schackno Act, a proposal for the extension of the mortgage and participation certificates and a reduction of the interest requirements (R. 9). With the consent of the Debtor and the holders of two-thirds in principal amount of the certificates, this proposal was approved by the Supreme Court of Kings County, New York, on December 6, 1934 (R. 52); Title Guarantee & Trust Company and the Debtor then entered into the extension agreement necessary to give effect to the terms of the Superintendent's proposal. Under this agreement the mortgage was extended to December 1, 1937,

upon condition that the Debtor pay interest at the contract rate of 6% per annum to December 1, 1934, and thereafter at 5% to December 1, 1937 (R. 10). Second, in order to provide a permanent administration of the trust estate, The Mortgage Commission promulgated a proposal for the appointment of a trustee for certificate holders (R. 11). On December 6, 1938, with the required consent of the certificate holders, the state court approved this proposal and designated the Mortgage Corporation of New York (to which the respondent Manufacturers Trust Company is successor by merger) as trustee (R. 38). The declaration of Trust (R. 22) created a trust estate consisting of the bond and mortgage and vested in the trustee "all the rights and powers of an absolute owner of the property * * *." The Declaration contained an enumeration of comprehensive powers; but it provided also that the trustee should not extend the bond and mortgage, reduce the rate of interest, release any property, or sell the securities or the property, without the permission of the court by order obtained after ten days' notice by mail addressed to the certificate holders. The order of the state court appointing the trustee (R. 38) also provided:

> Ordered that this Court, having assumed jurisdiction of this proceeding, shall retain jurisdiction hereof until the complete liquidation of the Trust Estate and the termi-

nation of the trust; and the Trustee, or any other interested party herein, may apply at the foot of this Final Order upon such notice as the Court may direct for such other and further relief as to the Court may seem just and proper.

By September 1939, trustees had been appointed in substantially similar fashion for all but a negligible fraction of the mortgages and properties which had come into the hands of the Mortgage Commission,[10] and that Commission's existence was terminated.[11] In each instance, the appointment of trustees for a certificated issue served as a complete fulfillment of the purposes of the temporary[12] Schackno and Mortgage Commission Acts. Since their appointment, and in accordance with the terms of their declarations of trust, the trustees have serviced the mortgages, distributing available proceeds to certificate holders and accounting annually to the courts of appointment.[13] New defaults on the part of mortgagors were encountered either by reason of the expiration of the interim extension agreements or because of an

[10] Final Report, Mortgage Commission, at p. 5.

[11] The Mortgage Commission Act was amended in 1939 (L. 1939, c. 944) so as to terminate the Commission in September 1939, and transfer its duties and powers under that Act to the Superintendent of Insurance.

[12] The effectiveness of the Schackno and Mortgage Commission Acts has been continued in force from time to time by amendments; both Acts expire July 1, 1943 (L. 1942, cc. 315, 638).

[13] Final Report, Mortgage Commission, at p. 7.

inability to meet the fixed charges under them. These situations the trustees have met either by foreclosure of the certificated mortgages or by negotiating with the mortgagors for a new extension or modification and submitting the negotiated agreements to the courts of appointment for approval whenever required by their declarations of trust."[14]

Thus, in the present case, the principal of the first mortgage was not paid at its extended maturity in 1937 and remained an "open" mortgage under the statutory moratorium.[15] The Debtor made all other payments due under the 1934 extension agreement until April 1, 1941, when it defaulted in payment of interest and taxes (R. 12). On numerous occasions, both before and after default, the Debtor and The Mortgage Corporation of New York negotiated for an agreement of further extension and modification which the trustee could, pursuant to the declaration of trust, submit to the court for approval (R. 62). On October 11, 1940, the Debtor submitted to the respondent mortgage trustee a proposal that the mortgage be extended for five years, with interest reduced to 4% per annum, and with amor-

[14] *Id.* at pp. 8, 9.

[15] By statute, foreclosure for principal defaults was suspended in New York for an emergency period (L. 1933, c. 793). The emergency period has been extended by amendment and now expires July 1, 1943 (L. 1941, c. 782).

tization at 2% per annum. This the trustee declined to entertain, taking the position that interest should be at the rate of 4½% per annum. The Debtor's proposal was never submitted to the court or to the certificate holders. (R. 14.)

On May 1, 1941, the mortgage trustee began foreclosure proceedings in the Supreme Court, Kings County; a receiver was appointed and entered into possession of the mortgaged property (R. 12). On August 11, 1941, while the foreclosure proceeding was pending in its initial stages, the Debtor again submitted to the mortgage trustee a proposal that the mortgage be extended for five years, with interest at 4½% and amortization at 1½%. The trustee rejected this proposal and did not submit it to certificate holders or to the court of appointment (R. 14).

The Debtor then filed its voluntary petition under Chapter X of the Bankruptcy Act on September 17, 1941 (R. 76). The petition was approved on the same day and reorganization trustees appointed by the District Court (R. 96). Thereafter, the mortgage trustee applied to the District Court to vacate the order of approval and dismiss the petition as not filed in good faith (R. 7).

The District Court denied the application (R. 4, 70). The Circuit Court of Appeals reversed (R. 111), Judge Frank dissenting.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred—

(1) In holding that the Debtor's petition was not filed in good faith.

(2) In directing the District Court to dismiss the petition.

SUMMARY OF ARGUMENT

I

The Debtor's petition was not lacking in good faith within the meaning of Section 146 (4). That section precludes a petition under Chapter X only in the event that there are prior pending proceedings which best subserve the interests of the creditors and stockholders. The proceedings pending in the New York courts do not satisfy the requirement that they best subserve the interests of the creditors and stockholders in this case.

The Schackno Act, under which the state court proceedings were pending, is not, in contrast to Chapter X, a vehicle for the reorganization of debtor corporations in which public investors are interested, but rather is concerned primarily with the relationship of holders of certificated mortgages *inter sese* and their relationship to the guarantors of the mortgage. Many of the usual incidents of proceedings for the reorganization of debtors are lacking in the Schackno Act and its later complement, the Mortgage Commission Act. Thus the debtor and its property are amenable to the juris-

diction of the state tribunal only upon the debtor's consent, and the state procedure prescribes no means for securing adherence to standards of fairness in proposed plans. Where fairness requires that junior claimants relinquish their interests, separate foreclosure proceedings or voluntary relinquishments are the only alternatives.

This case exemplifies the inadequacies of the state procedures. The available remedies provided by the Schackno and Mortgage Commission Acts had been exhausted, negotiations between the Debtor and the trustee appointed under the latter Act had broken down over the interest and amortization rates, and separate foreclosure proceedings had been begun.

The nature and procedures of Chapter X, on the other hand, stand in sharp contrast. That chapter is designed for the permanent rehabilitation of a corporate debtor while safeguarding the interests of security holders. Provision is made for a disinterested trustee, for expert assistance through the Securities and Exchange Commission, for full disclosure to security holders, and for other safeguards, few of which are present in the state procedures. It is plain, therefore, that neither the state court procedure nor the history of the Debtor's attempts at adjustment thereunder warrants the conclusion that the interest of investors would best be served by dismissal of the Debtor's petition.

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H

The Debtor's conduct in failing to seek further relief in the state court after it had assented to an extension therein did not constitute such lack of good faith as to require dismissal of its petition. To hold that mere participation in pending proceedings bars a petition under Chapter X is to overlook the fact that under Section 146 (4) prior pending proceedings are to bar such a petition only if such proceedings best subserve the interests of the creditors and stockholders.

But in any event, the Debtor was not personally disqualified from filing the petition. A debtor's conduct prior to the Chapter X petition should carry little weight in Chapter X proceedings since the right of creditors to be protected is paramount and since a debtor does not ordinarily remain in possession, but rather control of the proceedings passes to the court and disinterested trustees. Even if, however, prior conduct may in some instances constitute lack of good faith, it is plain, under applicable authorities, that the prior conduct here was not of such a character. The debtor is given the right to pursue its remedy under Chapter X; its participation in the state proceedings had been limited and incidental; and the state proceedings had, for all practical purposes of reorganization, run their course. Accordingly, even under broad standards of the term "good faith," the Debtor was not barred by his conduct from filing a Chapter X petition.

ARGUMENT

THE DEBTOR'S PETITION WAS NOT LACKING IN GOOD FAITH WITHIN THE MEANING OF THE ACT

Introductory.—The federal bankruptcy power is, of course, paramount over competing prior proceedings pending either in state or federal courts. Cf. *International Shoe Company* v. *Pinkus*, 278 U. S. 261; *Stellwagen* v. *Clum*, 245 U. S. 605. This principle of paramountcy is expressly reaffirmed and embodied in Chapter X, which provides not only that the institution of specified proceedings constitutes a substitute for an act of bankruptcy permitting creditors to petition for relief under Chapter X,[16] but also that—

> A petition may be filed under this chapter notwithstanding the pendency of a prior mortgage foreclosure, equity, or other proceeding in a court of the United States or of any state in which a receiver or trustee of all or any part of the property of a debtor has been appointed or for whose appointment an application has been made.[17]

Congress did not, however, exercise the paramount federal power to the exclusion of every other legal process. While the pendency of other proceedings alone is no bar to the assump-

[16] Bankruptcy Act, Sec. 3 (a) (4), (5), 3b, 102, 131; 11 U. S. C. 21a (4), (5), 21b, 502, 531.

[17] Bankruptcy Act, Sec. 256, 11 U. S. C. 656.

tion of jurisdiction by the reorganization court,[18] Congress nevertheless provided, by Section 141, that such jurisdiction should not be exercised unless a proceeding under Chapter X were instituted in good faith. And, further, in order to preclude utilization of Chapter X in such a manner as to defeat rather than accomplish the objective of protecting public investors, Congress provided in Section 146 (4) that a petition is not to be deemed as filed in good faith where another court proceeding is pending "and it appears that the interests of the creditors and stockholders would be best subserved in such proceedings."

In this case, the Debtor was involved in state court proceedings only in a limited sense; its property was never *in custodia legis* until 1941 when receivers were appointed in the foreclosure proceeding. The state court proceedings were not primarily concerned with the Debtor at all, but had been instituted in August 1933 by the Superintendent of Insurance in order to rehabilitate the guarantor of the first mortgage of the Debtor's property. In order to preserve the mortgage, the Superintendent proposed extension of the mortgage and modification of its requirements. The holders of the certificates and the Debtor consented to the proposal and entered into an agreement effectuating the proposal. While other events occurred subsequently—the

[18] The court below held that there was jurisdiction in this case (R. 111). See also *Brooklyn Trust Company* v. *Rembaugh*, 110 F. (2d) 838, 840 (C. C. A. 2).

creation by the state court in 1938 of a trust estate and appointment of a trustee, continued but unsuccessful negotiations between the Debtor and the trustee relative to further extension and modification of the mortgage, and finally, institution by the trustee of foreclosure proceedings and appointment of a receiver—two facts are outstanding. First, the Debtor was at no time the prime mover in the state court proceedings, and, indeed, its only participation, other than the fruitless negotiations directly with the trustee concerning the terms of the mortgage, was its consent to the Superintendent's proposal in 1934 to extend and modify the mortgage. Second, no comprehensive reorganization was ever submitted to the state court, none was discussed, and, indeed, no party, either the Debtor, the trustee, or any creditor, came forward with a plan. From 1933, when rehabilitation of the guarantor was begun, until 1941, when this case was instituted, no plan for the reorganization of the Debtor was, so far as the record shows, even contemplated. The state court "reorganization" during the entire time comprised only the 1934 extension and modification of the mortgage, the appointment of the trustee in 1938, and the abortive subsequent efforts by the Debtor to obtain further extension and modification, which never reached the state court.

Upon the basis of these circumstances, a majority of the court below held that the Debtor's petition for reorganization under Chapter X must be

dismissed because it was not filed in good faith. The precise basis of its conclusion is not wholly clear: The court seems to have held that Section 146 (4), relating to prior proceedings, did not govern this case; on the other hand, it also held that there was no absence of good faith "in the broad meaning of those words" (R. 111). Rather, the court held, there was a "special instance of lack of good faith flowing from the personal disqualification of the debtor" (R. 111). In the court's view, such "personal disqualification" apparently lay in the Debtor's assent to the 1934 modification and extension of the mortgage, and its subsequent payment to the trustee in conformity with the revised terms (R. 110).[19]

[19] That it was the "assent" or participation of the debtor in the state court proceedings which constituted the governing circumstance appears from a comparison of *Brooklyn Trust Company* v. *Rembaugh*, 110 F. (2d) 838 (C. C. A. 2), and *In re Castle Beach Apartments, Inc.*, 113 F. (2d) 762 (C. C. A. 2). In the *Rembaugh* case, the debtor had "assented" to the "reorganization" of the mortgage (*i. e.*, to the appointment of the trustee) and was, accordingly, held to be "in the position of one who voluntarily submitted the plan for the reorganization in the state court" (p. 840); accordingly, the debtor's petition under Chapter X was dismissed as not filed in good faith. In the *Castle Beach* case, on the other hand, although there was a similar state court "reorganization" proceeding, the debtor, who had purchased the property from the owner who had originally mortgaged the property, was not a "party" to the state court proceedings. The court held that the petition was filed in good faith, stating (p. 763) that there had been no state court proceeding for the reorganization of the debtor and "even had there been, that alone would not have been adequate ground for the dismissal of the petition."

We submit, however, that lack of good faith cannot be found in this case to arise either from the pendency of prior proceedings within the meaning of Section 146 (4) or in a "personal disqualification" supposedly resulting from the Debtor's conduct in assenting to a proposal made in the state court proceedings. Neither of these factors is such as to require the bankruptcy court's surrender of its paramount jurisdiction.

A

The petition cannot be deemed not to have been filed in good faith merely because of the existence of prior proceeding, since the interests of creditors and stockholders would not be best subserved in such prior proceeding

Under the terms of Section 146 (4), the fact that prior proceedings are pending precludes the invocation of Chapter X only in the event that such proceedings best subserve the interests of creditors and stockholders of the debtor. We submit that the court below was correct in holding (R. 111) that good faith was not lacking within the meaning of that subsection.

To determine whether or not prior pending proceedings will best subserve the interests of creditors and stockholders, it is necessary to compare the procedures available under such proceedings and those available under Chapter X. The comparison readily establishes that the state court proceedings here involved were not such as to fulfill the requirements of Section 146 (4).

Initially, it should be noted that Chapter X and the procedures provided under the New York laws differ fundamentally in purpose and in their fields of application and operation. They are not designed to attain the same, or even substantially similar, objectives.

Chapter X is a vehicle for the reorganization of debtor corporations in which public investors are interested. The Schackno Act, on the other hand, is only incidentally concerned with the debtor at all; its primary concern is the relationship of holders of certificated mortgages *inter sese* and their relationship to the companies which had guaranteed the mortgages.[20] It is an emergency measure designed to provide a procedure which would enable holders of certificated mortgage investments, through the agency of the Superintendent of Insurance, to modify their claims against their primary obligors (the mortgage debtors) without impairing their claims against the guarantee companies. For this purpose, the Act provided that with the approval of the state court a modification or extension of the mortgage to

[20] "* * * the Schackno Act is designed, not for the relief of the debtor and its creditors, but for the reorganization or rehabilitation of the certificate holders of a mortgage. It may well be that that act provides a comprehensive scheme for the reorganization of certificated mortgages, but there the relief stops." *In re Coney Island Hotel Corp.*, 9 F. Supp. 329, 332 (E. D. N. Y.), reversed on other grounds, 76 F. (2d) 126 (C. C. A. 2).

which two-thirds of the certificate holders assented, which was found to be fair, would become binding upon all certificate holders; it cannot, however, be made binding upon mortgagors without their consent. Although this procedure, therefore, bears some similarity to a reorganization device, it is more significant that, except as here noted, all of the usual incidents of proceedings for the reorganization of debtors are lacking.[21] Thus, neither the debtor nor its property becomes amenable, save upon consent, to the jurisdiction either of the Superintendent or the

[21] Accordingly, we submit that the Schackno Act and Mortgage Commission Act proceedings should not even be deemed "prior proceedings" for the purpose of determining good faith under Chapter X. In enacting Section 146, Congress intended to codify judicial interpretations of the general "good faith" provision of Section 77B. (See S. Rep. No. 1916, 75th Cong., 3rd Sess. (1938) at p. 27.) Moreover, Congress has, by specific enumeration elsewhere in Chapter X, attributed to the words "prior proceeding" a connotation similar to that found in the good faith cases under Section 77B. See Sections 113, 131, 148, 256 (11 U. S. C. A. 513, 531, 548, 656). In the concept employed in those cases, the phrase "prior proceeding" had reference only to a proceeding in which the assets of a debtor were *in custodia legis* for the primary purpose of rehabilitation or distribution for the benefit of claimants. See, for example, *In re Wixin & Golub, Inc.*, 84 F. (2d) 1 (C. C. A. 2); *Hickey v. The Ritz-Carlton Restaurant & Hotel Co., of Atlantic City*, 96 F. (2d) 748 (C. C. A. 3); *Brockett* v. *Winkle Terra Cotta Co.*, 81 F. (2d) 949 (C. C. A. 8); *Snyder* v. *Fenner*, 101 F. (2d) 736 (C. C. A. 3); *In re Knickerbocker Hotel Co.*, 81 F. (2d) 981 (C. C. A. 7). By this standard the state proceedings are not "prior proceedings" within the meaning of the statute.

state tribunal, nor is provision made for the proof and allowance of claims or for the recovery of assets fraudulently conveyed. The only coercive remedies available to certificate holders, or to the Superintendent, against the recalcitrant mortgagor are to be had outside the framework of the Act through conventional legal or equitable process, primarily foreclosure.

The Shackno Act was supplemented in 1935 by the Mortgage Commission Act, which established the Mortgage Commission of the State of New York as the independent statutory representative of certificate holders, and provided an alternative procedure which included provision for the appointment of permanent trustees.[22] These trustees were to acquire from the Mortgage Commission (as successor in this respect to the Superintendent of Insurance) the underlying bonds and mortgages securing the certificated mortgage investments and were to administer the assets thus acquired for the ratable benefit of the certificate holders.

The trusts resulting from the operations of the provisions of the Mortgage Commission Act have been carried out under separate declarations of

[22] Although plans to become effective under the Schackno Act require the affirmative assent of two-thirds of certificate holders, plans may be made effective under the Mortgage Commission Act unless one-third of the certificate holders register a positive dissent. Mortgage Commission Act [L. 1935, c. 19 as amended], Section 7.

trust which follow generally a standard form, although the pattern has varied in detail among the different counties in New York State.[23] The trustees are vested under the trust instrument with all the rights and powers of absolute owners of the certificated bonds and mortgages, and the trusts continue until the assets in the estate have been fully liquidated. Once permanent trustees are appointed, the emergency legislation has fully served its purposes as related to the administration of certificated issues; thereafter the trustees function under the powers delegated to them by the declaration of trust. Their powers pursuant to these declarations are limited only to the extent that extensions of the bond and mortgage, reductions in interest, and sales of securities and properties covered thereby, require the permission of the court. Thus, the whole proceeding is similar in nature to a proceeding in which the estate holding mortgage securities in the estate applies for instructions concerning a proposed agreement with the mortgagor. The fiduciary deals with the mortgagor as an outsider, and the court proceedings merely provide sanction for the fiduciary's action. And although the declarations of trust usually require that the court's approval be upon notice to security holders, there is no requirement that the

[23] See Spitz, *The Administration of Guaranteed Mortgage Trusts*, contributed article, N. Y. Law Journal, Jan. 6, 7, 8, 1942.

security holders accept the trustees' proposals by special vote.[24]

Plans approved under the Schackno or Mortgage Commission Acts, and presumably those approved pursuant to declarations of trust, must conform to the requirement that they be fair, reasonable, and equitable to the holders of the mortgage investments. However, the state procedures provide no means for securing adherence to this standard if it is to be given the content which it has in the Bankruptcy Act. *Case* v. *Los Angeles Lumber Products Co., Ltd.*, 308 U. S. 106; *Consolidated Rock Products Co.* v. *DuBois*, 312 U. S. 510. Where compliance with the standard of "fairness" requires that the junior claimants relinquish the whole or a portion of their interest, separate foreclosure proceedings are the only available alternatives to voluntary concessions by such claimants. This inadequacy of the state procedures has of necessity induced plans which, in the main, provide for short extensions of the mortgage, reduction of interest rates, suspension of

[24] See S. E. C. Protective Committee Study, Vol. VI, p. 188. Under some declarations of trust, proposals for extension of mortgage for less than a specified number of years may be effectuated by the trustees without notice to security holders and without application for the approval of the state court. For example, the declaration of trust in *In re Paloma Estates, Inc.*, 126 F. (2d) 72 (C. C. A. 2), petition for certiorari filed May 12, 1942, No. 89, this Term, provides for notice to security holders only when the proposed extension is for more than three years and the court directs that such notice be given.

amortization payments, and the like, without compensatory advantage to senior claimants.[25] Cf. *Consolidated Rock Products Co.* v. *DuBois, supra.* Furthermore, there is no mandatory requirement of feasibility, and the plans of the type just described have the frequent consequence that, at the end of the period of extension, neither payment nor refunding of the mortgage is possible,[26] and resort to further proceedings must be had.

The instant case exemplifies the inadequacies of the state procedures. The bond and mortgage are now held by Manufacturers Trust Company (as successor to The Mortgage Corporation of New York) pursuant to the declaration of trust created in 1938 (R. 38). Under the broad powers granted to the trustee (R. 22), negotiations were conducted with the Debtor looking to a new extension and modification of the mortgage to replace the three-year extension which expired in 1937. Although the mortgage trustee acknowledged the "top heavy" condition of the mortgage (R. 20), it never proposed or attempted to consummate any more feasible or permanent reorganization than an extension, with the added feature of a 2%

[25] Annual Report, Mortgage Commission, at p. 5; cf. Alger Report at p. 78.

[26] See *Brooklyn Trust Company* v. *Rembaugh*, 110 F. (2d) 838 (C. C. A. 2); *In re Paloma Estates, Inc.*, 126 F. (2d) 72 (C. C. A. 2), petition for certiorari filed May 12, 1942, No. 89, this Term; *In re Castle Beach Apartments, Inc.*, 113 F. (2d) 762 (C. C. A. 2); *In re Blinrig Realty Corp.*, 114 F. (2d) 100 (C. C. A. 2).

annual amortization of principal (R. 14), and the break-down in negotiations with the debtor resulted from disagreement merely as to whether the aggregate amortization and interest rate should be 6 or 6½% per annum.

The remedies afforded by the Schackno and Mortgage Commission Act procedure and the resulting trust procedure, all of which require an agreement with the debtor, had thus been exhausted, and the trustee has instituted foreclosure proceedings. It is apparent, however, that the foreclosure must either end in a forced sale, the result of which for the security holders is a matter of extreme uncertainty, or it must serve as the procedural vehicle for a reorganization according to the well-known pattern of equity receiverships.[27] But it was this very type of inadequate equity procedure which Chapter X, and its predecessor, Section 77B, were designed to supplant. See *Securities and Exchange Commission* v. *United States Realty & Improvement Co.*, 310 U. S. 434, 448.

[27] There can be no contention that the foreclosure proceeding has progressed so far that the maintenance of the Chapter X petition would have been adverse to the interests of the investors, since no plan had been approved or even promulgated, nor other similar definitive step completed in the foreclosure proceeding at the time the petition under Chapter X was filed. Cf. *In re Mt. Forest Fur Farms of America*, 103 F. (2d) 69 (C. C. A. 6), certiorari denied, 308 U. S. 583; *In re Surf Bldg. Corp.*, 11 F. Supp. 295 (E. D. Ill.); *In re Prairie Avenue Bldg. Corp.*, 11 F. Supp. 125 (E. D. Ill.).

The nature and procedures of Chapter X of the Bankruptcy Act stand in sharp contrast to those provided by the New York acts. In Chapter X, Congress provided the procedure which appeared, after exhaustive inquiry,[28] best designed for the permanent rehabilitation of debtor corporations and the protection of the interests of the investors. This Court has, in the *United States Realty & Improvement Co.* case (*supra*, at pp. 449–453) recently appraised the features of Chapter X designed to make it an adequate vehicle for the reorganization of corporations in which public investors are interested. As was there observed, Chapter X safeguards the interests of security holders while providing an adequate remedy for the permanent reliabilitation of a corporate debtor. Provision is made *inter alia* for the appointment of a disinterested trustee who will investigate and report concerning the debtor's financial and managerial problems; for securing "impartial and expert administrative assistance" through participation in the proceedings by the Securities and Exchange Commission (*id.*, 449); for assurance that security holders will not be required to vote on any proposed plan of reorganization until they

[28] S. Rep. No. 1916, 75th Cong., 3rd Sess. (1938); H. Rep. No. 1409, 75th Cong., 1st Sess. (1937); S. E. C. Report on the Study and Investigation of the Work, Activities, Personnel and Functions of Protective and Reorganization Committees, Parts I–VIII.

have received full information concerning the plan[29] and until the plan has been initially approved by the court as fair and equitable;[30] and for "control by the court over security holders' committees and the formulation of reorganization plans" (*ibid.*).

The state court procedures provide practically none of the basic safeguards to be found in Chapter X for the protection of investors. There is no provision for the appointment of a disinterested trustee charged with the investigatory and reporting functions imposed by Section 167 of the Bankruptcy Act; there is no provision authorizing participation in the proceedings by a permanent administrative agency adequately staffed;[31] there is no requirement that a plan must be found

[29] Bankruptcy Act, Sec. 175, 11 U. S. C. 575.

[30] Bankruptcy Act, Sec. 176, 11 U. S. C. 576.

[31] The state court justices having jurisdiction over the procedures applicable to guaranteed certificated mortgage issues were authorized in 1940 [Ch. 764 of the New York Laws of 1940, amending Section 17a of the Mortgage Commission Act; N. Y. Unconsolidated Laws, Section 1768] to select certain persons and endow them with the customary powers of a state court referee, for the purpose of aiding the courts in supervising the functionings of trust estates created under the Mortgage Commission Act. On May 10, 1940, the justice handling certificated mortgages in the Second Judicial Department of the State (comprising the counties of Kings, Queens, Nassau, Suffolk, and Richmond) by order appointed James F. Donlan, Esq., for such purpose in that Department, and for convenience designated Mr. Donlan's office as the "Bureau of Trust Supervision." We have been unable to find any published material relating to this office and describing its mechanics and activities.

to be fair and equitable and feasible and approved by the court before the assent of security holders may be solicited, or that information adequate to supply a basis for an informed judgment be furnished to security holders in connection with such solicitation. Wholly absent also are the safeguarding provisions found in Section 216, subdivisions (10), (11), (13),[32] relating to the form and substance of reorganization plans. In sum, the superiority of Chapter X over the state procedures is even clearer than its superiority over Chapter XI of the Bankruptcy Act. See *Securities and Exchange Commission* v. *United States Realty & Improvement Co., supra.* See also Note (1934) 34 Col. L. Rev. 663; Note (1935) 35 Col. L. Rev. 874; Note (1941) 18 N. Y. U. L. Quarterly Review 339, 418; Siegel, *Chapter X or Schackno Act Proceedings* (1941) 27 Corn. L. Q. 56.

It is plain, therefore, that neither the state court procedure here involved nor the actual history of the attempts at adjustment warrants the conclusion that the interests of investors would best be served by the dismissal of the Debtor's petition under Chapter X.[33]

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[32] 11 U. S. C. 616 (10), (11), (13).

[33] Section 146, in defining good faith, was intended by Congress to be a "codification" of some of the judicial interpretations of that phrase under Section 77B. See S. Rep. 1916, 75th Cong., 3rd Sess. (1938), p. 27. See also *supra*, note 21. And it is clear that the instant case falls within that category of decisions holding that no lack of good faith arose from the pendency of prior proceedings. See e. g.,

B

The debtor's conduct did not constitute lack of good faith so as to require dismissal of the petition

While Section 146 defines four situations in which a petition for reorganization under Chapter X shall be deemed not to have been filed in good faith,[36] it also provides that these definitions shall not limit "the generality of the term 'good

In re Cloisters Bldg. Corp., 79 F. (2d) 694 (C. C. A. 7), certiorari denied, 296 U. S. 657; *In re Knickerbocker Hotel Co.*, 81 F. (2d) 981 (C. C. A. 7); *Union National Bank v. Lehmann-Higginson Grocer Co.*, 82 F. (2d) 969 (C. C. A. 10); *In re South Coast Co.*, 8 F. Supp. 43 (D. Del.); *In re Prairie Ave. Bldg. Corp.*, 11 F. Supp. 125 (E. D. Ill.); *In re Surf Bldg. Corp.*, 11 F. Supp. 295 (E. D. Ill.). In special circumstances, of course, Section 77B proceedings were held not to supersede pending state court proceedings. See e. g., *In re Electric Public Service Co.*, 9 F. Supp. 128 (D. Del.) (petition dismissed where state court had already approved a plan of reorganization in a pending receivership proceeding and receiver had already sold all assets pursuant to the plan); *In re Williamsport Wire Rope Co.*, 10 F. Supp. 481 (M. D. Pa.), appeal dismissed, *Williamsport Wire Rope Co. v. Bethlehem Steel Corp.*, 78 F. (2d) 1023 (C. C. A. 3) (petition dismissed where plan had already been partially consummated in state court receivership proceeding and plan proposed by petitioner under Section 77B found not feasible, practicable, or acceptable). But plainly the facts of these latter cases are not comparable to those presented here.

[36] The petition shall be deemed not to have been filed in good faith if (1) the petitioning creditors have acquired their claims for the purpose of filing the petition; (2) adequate relief would be obtainable under Chapter XI; (3) it is unreasonable to expect that a plan of reorganization can be effected; or (4) a prior pending proceeding would best subserve the interests of creditors and stockholders.

faith' ". Although the court below held that there was no "absence of good faith * * * in the broad meaning of those words" (R. 111), it must have been proceeding under the "generality" clause, for it undertook to direct dismissal of the petition because of an asserted "lack of good faith flowing from the personal disqualification of the debtor", (*ibid*). This "personal disqualification" the court apparently found to arise because the Debtor had once consented to an extension of the mortgage, approved by the state court, and had not applied to the state court for further relief after the extension expired. This conclusion, we believe, overlooks the express statutory standards and is clearly erroneous.

Although for the sake of convenience, in order to follow the treatment of the issue by the court below, we discuss the issue of "personal disqualification" as separate from the question whether there was a lack of good faith within the meaning of subsection (4) (see Point A, *supra*), we state initially the view that such a dichotomy is, for present purposes, unreal. In enacting subsection (4), Congress clearly intended a comprehensive definition of the circumstances in which resort to Chapter X is to be precluded by the pendency of prior proceedings. Whatever lack of good faith there may be here, and we suggest there is none, clearly arises out of the prior proceedings. Therefore, if the assumed lack of good faith is to bar resort to Chapter X, it must be coupled, we submit, with

the further circumstance that the prior proceedings best serve the interests of the creditors and stockholders; otherwise the Chapter X petition is not, for that reason, vulnerable. Were the decision of the court below to be accepted, Section 146 (4) would thereby be modified to provide in effect that a petition is to be deemed not filed in good faith *either* if the prior pending proceedings best serve the interests of creditors or stockholders, *or, regardless of the interests of creditors and stockholders,* if the debtor actively participated in such proceedings. An amendment of this nature would eliminate the former express standard, since, except in rare instances,[35] it is difficult to envisage cases in which the debtor did not in some way participate in the prior pending proceedings.

But apart from this factor, we submit that in any event the Debtor's conduct did not constitute bad faith.

Initially, it is important to note that the concept of bad faith in the sense of personal disqualification of a petitioning debtor must, because of the nature of Chapter X, play a highly restricted role. Whether or not personal disqualification of a *debtor* might deprive it of "its legal right to

[35] In *In re Castle Beach Apartments, Inc.*, 113 F. (2d) 702 (C. C. A. 2), the petitioning debtor was held not to be disqualified; he had participated in the state court proceedings only to the extent that he had subsequently purchased the property from the original debtor-owner in connection with a foreclosure proceeding. See *supra*, note 19.

have its property administered in bankruptcy,"[36] the right of *investors* to have their interests protected by the remedial provisions of Chapter X should not normally be abridged. Indeed, "personal disqualification" appears to have no place in those Chapter X proceedings in which the debtor is not to remain in possession.[37] Personal disqualification may have had some relevance in cases under Section 77B or in "friendly receiverships," for in those proceedings the intentions and motives of the debtor who instituted the proceedings were significant because of the continuing dominance of those controlling the debtor in the administration of the estate and because of "the power of the old management to play a role in the formulation of the plan."[38] But these factors are absent under Chapter X. The decisions of this Court in *Case* v. *Los Angeles Lumber Products Co., Ltd.*, 308 U. S. 106, and *Consolidated Rock Products Co.* v. *DuBois*, 312 U. S. 510, and the express provisions of Chapter X, make clear that an improper motive of the debtor need be no obstacle to the successful prosecution of the proceedings in the interests of security holders. In pro-

[36] *In re Koch*, 116 F. (2d) 243, 247 (C. C. A. 2).

[37] In all cases where the debtor's liabilities exceed $250,000, a trustee must be appointed; in cases involving smaller liability the judge may appoint a trustee or may continue the debtor in possession. Bankruptcy Act, Sec. 156; 11 U. S. C. 556.

[38] Circuit Court Judge Frank dissenting (R. 122).

ceedings under Chapter X, upon the approval of the petition, control of the debtor's property and of the proceedings passes from the debtor to the court and its trustee and, in a measure, to the security holders; the debtor as such no longer plays a dominant role in the proceedings. *In re Porto Rican American Tobacco Co.*, 112 F. (2d) 655 (C. C. A. 2). Indeed, the more questionable may be the motives of the debtor, or those who control it, the more need there may be for the bankruptcy court to assert its comprehensive jurisdiction and make available to investors the remedies and safeguards of Chapter X.

Accordingly, the concept of personal disqualification of the debtor is of doubtful applicability under Chapter X in any circumstances.[39] See Note (1941) 18 N. Y. U. L. Quarterly Review 399, 412–413; cf. Finletter, *The Law of Bankruptcy Reorganizations* (1939), pp. 75, 77–78; Note (1934) 48 Harv. L. Rev. 283, 284, n. 2. Since, therefore, the very nature of a Chapter X proceeding requires an interpretation of personal disqualification constituting bad faith far narrower than that warranted in equity receiverships and in Section

[39] Thus it has been suggested that even *In re Wisan & Golub*, 84 F. (2d) 1 (C. C. A. 2), where a debtor's petition under Section 77B was held not to have been filed in good faith because the debtor had concealed its assets, is not applicable to Chapter X proceedings. Note (1941), 18 N. Y. U. L. Quarterly Review 399, 413, n. 117; cf. Finletter, *The Law of Bankruptcy Reorganizations* (1939), p. 75.

77B cases, the court below attached undue significance to the asserted personal disqualification.

But in any event, the Debtor's conduct, if tested by the standards obtaining under the older types of proceedings, would not constitute a personal disqualification. The mere fact of a debtor's filing a petition under the Bankruptcy Act when some state proceeding might be available does not constitute bad faith. And as this Court has held in a proceeding under Section 75 (s) of the Bankruptcy Act, a debtor should not be charged with bad faith because he takes the course provided for him by Congress. *John Hancock Mutual Life Insurance Co.* v. *Bartels*, 308 U. S. 180, 185. On the same basis, *i. e.*, that "bad faith cannot attach to adopting a course afforded by Congress," a debtor who was in a state court receivership has been held not to be disqualified from filing a petition under Section 77B. *In re South Coast Co.*, 8 F. Supp. 43, 45 (D. Del.).[*]

[*] It has been held, however, that circumstances may be such that resort to Section 77B is not in good faith. Thus in *In re Cook*, 104 F. (2d) 981 (C. C. A. 7), a creditor's petition was dismissed as not filed in good faith where the petitioning creditors, trustees under a bondholders' protective agreement, were defendants in a state court proceeding in which it had been alleged that they had engaged in fraudulent conduct and in which an injunction and accounting were sought. The trustees obtained a 60-day extension of time to render the accounting, but on the 50th day filed a petition under Section 77B. The evidence was

No different conclusion is warranted because the Debtor consented to the 1934 extension and modification of the mortgage and, in 1940 or thereafter, failed to present its limited proposal for further extension and modification to the state court after it had been rejected by the trustee. Whether the Debtor had the power itself to present an application to the state court for further relief is a question on which the majority of the court below and the district judge were in disagreement (see R. 110, 71–72, 74–75; see also dissenting opinion of Judge Clark in *In re Paloma Estates, Inc.*, 126 F. (2d) 72, 75). The Debtor itself clearly assumed that the state court's reservation of jurisdiction in the 1938 order (*supra*, pp. 8–9) did not empower it to make such an application (R. 62, 67–68). And even if we were to assume that the Debtor was empowered to apply directly

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held to show that the purpose of the petition under Section 77B was to escape the state court's order to account (p. 985). The court held that the petition was filed in bad faith, stating (*ibid.*) that its purpose was not to benefit a corporation in financial distress, but to "escape jurisdiction of another court where the day of reckoning of their alleged acts of misconduct was at hand." It is to be noted that a similar rule had been enunciated for ordinary bankruptcy proceedings, for the institution of which there was no statutory requirement of good faith. *Zeitinger* v. *Hargadine-McKittrick Dry Goods Co.*, 244 Fed. 719 (C. C. A. 8), certiorari denied, 245 U. S. 667. Whatever the applicability of these cases to Chapter X proceedings (see *supra*, pp. 32–35), it is clear that the petitioners' conduct and motives there are in no way comparable to the Debtor's conduct and motives here.

to the state court, it seems apparent that such a course would have been entirely futile, not only because of the flat opposition of the trustee (*supra*, pp. 10–11), but also because of the clear inappropriateness of the available state court proceedings for the task of comprehensive reorganization which appeared to be necessary (see R. 67–68, *supra*, pp. 21–26). In the light of these circumstances, it cannot be concluded that the Debtor's failure to apply to the state court for relief constituted a personal disqualification amounting to bad faith even under the most rigid interpretation of those terms.[41] Indeed, we have been unable to find any case involving Section 77B proceedings in which it was held that participation in state court proceedings *per se* disqualifies the debtor from resort to Section 77B. Rather, the contrary has been held. *Union National Bank* v. *Lehmann-Higginson Grocer Co.*, 82 F. (2d) 969 (C. C. A. 10) (Section 77B petition held filed in good faith although debtor had

[41] The earlier cases relating to good faith, some of which were intended by Congress to be codified in Section 146 (*supra*, p. 29, note 33) give no indication that "personal disqualification" can be found on the basis of mere failure to pursue state remedies, whether the availability of such remedies is doubtful, as here, or not. Those cases in which personal disqualification amounting to bad faith was found are wholly different in degree and kind from the situation here presented. See *e. g.*, *In re Cook*, *supra*; *In re Wisun & Golub*, *supra*; *Milwaukee Postal Bldg. Corp.* v. *McCann*, 95 F. (2d) 948 (C. C. A. 8) (debtor corporation organized solely to take advantage of Section 77B; *In re North Kenmore Bldg. Corp.*, 81 F. (2d) 656 (C. C. A. 7) (same); see also, Finletter, *op. cit. supra*, pp. 74–85.

consented to state order of prompt liquidation); cf. *Struthers Furnace Co.* v. *Grant*, 30 F. (2d) 576 (C. C. A. 6).[12]

Nor can there be any thought that the conclusion of the court below will better serve orderly and successful adjustments under the procedures provided by New York. For if it be true that a debtor's petition under Chapter X is barred by its participation in state proceedings, even such limited participation as occurred in this case, a premium will be placed upon avoidance and lack of cooperation by a debtor in state proceedings. Under the rule of the court below, its cooperation in such proceedings would thereafter forever bar it from resort to the remedies afforded by Chapter X.

[12] The *Struthers Furnace Co.* case involved an ordinary bankruptcy proceeding, for which there was no statutory requirement of good faith. Nevertheless, the court undertook to decide whether the bankruptcy proceeding should be dismissed for fraud since the petitioning debtor had voluntarily submitted to, and in part instituted, a state court receivership. The court refused to vacate the bankruptcy adjudication, stating (p. 577) that "It does not follow that the corporation itself is estopped from filing a voluntary petition. Indeed, in the interest of equality of distribution between creditors, or to prevent secured creditors from proving for their entire claim instead of only for the excess over the value of the securities, or to avoid what in bankruptcy would be preferences, it may well be the duty of the corporation to file a petition in bankruptcy, despite its prior consent to an equity receivership. * * *"

Even apart from these considerations, it appears that the court below misconceived the criteria embodied in Section 146 of the Act. Once a petition has been approved, the course of the proceedings under Chapter X is in no way dependent upon whether the petition has been filed by the debtor or by creditors. Logically, therefore, if personal disqualification of the debtor justifies a determination that its petition should not be approved, a similar disqualification would act as a bar to a petition by creditors in their own interests. Thus it would seem to follow that if the debtor were here disqualified from filing a petition, the same would be true of creditors who consented to the 1934 extension or otherwise participated in the state court proceedings. Nonetheless, the court below intimated that a petition could have been approved in this case had it been filed by the creditors (R. 111). By such a conclusion, the decision below is shown to reflect no consistent appraisal of the importance of conduct in a prior proceeding. This inconsistency stems from the failure of the court below to give adequate heed to the congressional purpose, shown specifically in Section 146 (4) and by the whole statutory scheme of Chapter X, that the primary test for entertaining the proceeding under the chapter is whether proceedings would best subserve the interests of creditors and stockholders.

CONCLUSION

The judgment of the court below should be reversed.

Respectfully submitted.

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SEPTEMBER 1942.

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FILE COPY

IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

No. ~~948~~ 24

MARINE HARBOR PROPERTIES, INC.,

Petitioner,

vs.

MANUFACTURERS TRUST COMPANY (successor by merger to The Mortgage Corporation of New York), as trustee for the benefit of certificate holders in mortgage guaranteed by Bond and Mortgage Guarantee Company, Guarantee #181,568,

MAURICE RUBINGER, trustee of Marine Harbor Properties, Inc.,

SAMUEL SILVERMAN, additional trustee of Marine Harbor Properties, Inc.,

MORTIMER RUBENSTEIN, Foreclosure-receiver,

and

SECURITIES AND EXCHANGE COMMISSION.

Brief of Respondent Manufacturers Trust Company, as Trustee, in Opposition to Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

No. 948

MARINE HARBOR PROPERTIES, INC.,

Petitioner,

vs.

MANUFACTURERS TRUST COMPANY (successor by merger to The Mortgage Corporation of New York), as trustee for the benefit of certificate holders in mortgage guaranteed by Bond and Mortgage Guarantee Company, Guarantee #181,568,

MAURICE RUBINGER, trustee of Marine Harbor Properties, Inc.,

SAMUEL SILVERMAN, additional trustee of Marine Harbor Properties, Inc.,

MORTIMER RUBENSTEIN, Foreclosure-receiver,

and

SECURITIES AND EXCHANGE COMMISSION.

Brief of Respondent Manufacturers Trust Company, as Trustee, in Opposition to Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit

STATEMENT AND OPINIONS BELOW

Marine Harbor Properties, Inc. (hereinafter referred to as the "debtor") has petitioned this court for the issu-

ance of a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit to review a decision of that court entered January 27, 1942, reversing an order of the United States District Court for the Southern District of New York which denied an application by The Mortgage Corporation of New York, as trustee (merged into Manufacturers Trust Company on September 30, 1941), to dismiss the debtor's petition for reorganization under Chapter X of the Bankruptcy Act and to vacate an *ex parte* order approving the debtor's petition. The opinion of the District Court (Bright, *D. J.*) is reported in 41 F. Supp. 814 (S. D. N. Y.). The majority opinion (Swan, *C. J.* and Chase, *C. J.*) and the dissenting opinion (Frank, *C. J.*) in the Circuit Court of Appeals have not yet been reported.

JURISDICTION

The decree of the Circuit Court of Appeals was entered on January 27, 1942 (R. 126). The petition for a writ of certiorari was filed on February 13, 1942. The jurisdiction of this court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925.

STATUTES INVOLVED

Section 141 of Chapter X of the Bankruptcy Act (11 U. S. C., Section 541) provides:

> "§ 541. PETITION OF DEBTOR
>
> Upon the filing of a petition by a debtor, the judge shall enter an order approving the petition, if satisfied that it complies with the requirements of this chapter and has been filed in good faith, or dismissing it if not so satisfied."

Section 146 (11 U. S. C., Section 546) provides in part as follows:

"§ 546. Good Faith of Petition

Without limiting the generality of the meaning of the term 'good faith', a petition shall be deemed not to be filed in good faith if—

* * * * * *

(3) It is unreasonable to expect that a plan of reorganization can be effected; or

(4) A prior proceeding is pending in any court and it appears that the interests of creditors and stockholders would be best subserved in such prior proceeding.".

STATEMENT OF THE CASE

The majority opinion (R. 106-111) gives a succinct and accurate summary of most of the facts, which will not be here repeated. Two salient facts must, however, be emphasized. First: It is undisputed that the value of the land and apartment house building, which is the debtor's sole asset and which secures the first mortgage (of which Manufacturers Trust Company is trustee for certificate holders), is not more than $350,000, while the amount of such mortgage with arrears of interest and taxes was $399,814.93 on October 1, 1941 (R. 15). Thus, entirely apart from the second, third and fourth mortgages and the balances due on conditional bills of sale, there is a deficit of approximately $50,000. Second: It is also undisputed that under the provisions of the final order of the state Supreme Court approving the appointment of The Mortgage Corporation of New York (now merged into this respondent) as trustee of the mortgage, not only the trustee but also the debtor had

the right to apply to that court for any relief to which it might have felt itself entitled (R. 44). Such final order, entered after court hearing upon notice to the debtor (R. 11) and with its acquiescence and upon the approval of at least 66⅔% in principal amount of certificate holders, provided in part as follows (R. 44):

> "ORDERED that this Court, having assumed jurisdiction of this proceeding, *shall retain jurisdiction hereof until the complete liquidation of the Trust Estate* and the termination of the trust; and the Trustee, or *any other interested party herein, may apply at the foot of this Final Order* upon such notice as the Court may direct *for such other and further relief as to the Court may seem just and proper.*"*

Under the declaration of trust, respondent as trustee is vested with "all the rights and powers of an absolute owner" (R. 24), but these broad powers are limited by Article III of the declaration, which provides (R. 26-27):

> "III. The Trustee shall not extend any bond and mortgage, reduce the rate of interest, release any property from any mortgage except as authorized by the terms thereof or the order above referred to, nor sell the securities or the property covered thereby, without the permission of the Court by order obtained in said reorganization proceeding after ten days' notice by mail addressed to the certificate holders."

The usual procedure is for the property owner to negotiate with the trustee, subject to state court approval, for further extensions and reductions of the mortgage until

*Italics in this brief are supplied unless otherwise noted.

eventually the mortgage can be liquidated or refinanced. So in this case, following the maturity of the mortgage on December 1, 1937, the debtor and the trustee carried on lengthy negotiations looking toward a feasible plan for the further extension and modification of the mortgage (R. 14-15). There was, as is usually the case, a difference of opinion between the debtor and the trustee as to the proper terms for a further extension; but the debtor, instead of availing itself of the privilege of going into the state court which had retained jurisdiction of the matter, with a suggestion for extension of the mortgage, wilfully defaulted in the payment of interest due April 1, 1941 and in the payment of real estate taxes due April 1, 1941. This default occurred at a time when the mortgage was running "open" under the New York Moratorium Laws (New York Civil Practice Act, Sections 1077-a *et seq.*), so that the debtor was simply required to pay taxes and interest at 5% but no amortization, and it occurred despite the fact that the earnings of the property were sufficient to cover taxes and interest (R. 16).

After the trustee's institution of the foreclosure action, the debtor further defaulted with respect to certain promises which it made for the clearing up of arrears and settlement of the foreclosure proceeding (R. 58-59). After the foreclosure action had proceeded for 4½ months with a state court receiver in possession, the debtor obtained an order *ex parte* approving its petition for "reorganization" under Chapter X (R. 13, 6).

THE ISSUE

The issue here is whether or not a mortgagor (debtor), who has no equity in the mortgaged property, and who has

participated in proceedings to reorganize a certificated mortgage in the state court under well established state court procedure and who is entitled to apply to such court in such proceeding for any relief, may ignore the pending state court reorganization and foreclosure proceedings and institute a proceeding in the federal court for "reorganization" under Chapter X.

ARGUMENT

The burden of debtor-petitioner's argument and of the dissenting opinion of the Circuit Court of Appeals is (1) that debtor's filing of a petition in the federal court, despite its utter lack of equity in the property and despite the pendency of the state court proceeding, is not indicative of any lack of good faith, and (2) that even if there was an absence of "good faith" on the part of the debtor the federal court should not dismiss the petition because the Chapter X proceeding might be for the benefit of creditors. Debtor objects to the conclusion of the majority opinion that—"The applicable principle * * * is not an absence of good faith in the filing of the new petition in the broad meaning of those words but a special instance of a lack of good faith flowing from the personal disqualification of the debtor." (R. 111) The basis of the decision of the majority appears, however, in the following two sentences of their opinion (R. 110):

> "But the debtor made no attempt to bring its proposals to the attention of the state court in the pending proceeding, as we think it was entitled to do as an 'interested party'; had it done so its proposals, with the court's approval, could have been presented to the certificate holders. That proceeding provides ade-

> quate means to reorganize the mortgage and protect the rights of all certificate holders whose interests alone exhaust the debtor's property."

It is true that the majority held that the petition should not be dismissed under Section 146, subdivision (3), and they did not hold that it should be dismissed specifically under Section 146, subdivision (4). They concluded that Section 146 does not limit the generality of the meaning of "good faith", which is required by Section 141 to be evidenced to the satisfaction of the court. This would seem to be a correct view, not only because of the express language of Sections 141 and 146, but also because of the general requirements of good faith contained in Sections 142, 143, 144 and in other sections of Chapter X.

We believe that it is immaterial in this case, whether the dismissal is predicated upon "a special instance of a lack of good faith" or upon lack of good faith as defined in subsections (3) or (4) of Section 146. The decisions of the courts show that they have exercised a broad discretion in determining whether or not petitions under Chapter X and its predecessor Section 77B should be dismissed because of lack of "good faith" in their filing.

In *Tennessee Pub. Co.* v. *Amer. Bank*, 299 U. S. 18, this Court, in affirming a dismissal of a petition under Section 77B,* stated (p. 22):

> "Nor do we need to inquire as to the precise limits of the concept of 'good faith' as required by § 77B. * * * However honest in its efforts the debtor may be, and however sincere its motives, the District Court is not bound to clog its docket with

*Section 141 of Chapter X is taken, almost verbatim, from Section 77B.

visionary or impracticable schemes for resuscitation."

In *Securities Comm'n* v. *U. S. Realty Co.*, 310 U. S. 434, this Court, after discussing the requirement of good faith, ruled that a petition filed under Chapter XI should be dismissed, although it fell directly and specifically within the literal provisions of that chapter, solely because the general public interest and purpose of the reorganization statutes required that such a petition should be filed under Chapter X rather than Chapter XI.

In *Chapman Bros. Co.* v. *Security First-Nat. Bank*, 111 F. (2d) 86 (C. C. A. 9), cert. den. 311 U. S. 652, the court affirmed the dismissal of a debtor's petition under Chapter X, on the ground that it lacked good faith. The mortgage on debtor's property exceeded the value of the mortgaged premises by approximately $1,000,000. See also *Seaboard Terminals Corp.* v. *Western Maryland Ry. Co.*, 108 F. (2d) 911 (C. C. A. 4) (where dismissal of petition under Chapter X was affirmed because of doubtful status of debtor's assets and hopelessness of effectuating any reorganization plan which might be submitted); *Wayne United Gas Co.* v. *Owens-Illinois Glass Co.*, 91 F. (2d) 827 (C. C. A. 4), reversed on other grounds 300 U. S. 131; *Reading Hotel Corp.* v. *Protective Committee, etc.*, 89 F. (2d) 53 (C. C. A. 3), cert. den. 302 U. S. 743; *Manati Sugar Co.* v. *Mock*, 75 F. (2d) 284 (C. C. A. 2); *Provident Mut. Life Ins. Co.* v. *University Ev. L. Church*, 90 F. (2d) 992 (C. C. A. 9); *O'Connor* v. *Mills*, 90 F. (2d) 665 (C. C. A. 8); *Price* v. *Spokane Silver & Lead Co.*, 97 F. (2d) 237 (C. C. A. 8), cert. den. 305 U. S. 626; *First Nat. Bank* v. *Conway Road Estates Co.*, 94 F. (2d) 736 (C. C.

A. 8), cert. den. 304 U. S. 578 (where the Circuit Court stated (p. 739): "Whenever want of good faith appears the debtor's petition should be dismissed even though a plan of reorganization has not been submitted.").

In *In re Suburban Properties*, 110 F. (2d) 438 (C. C. A. 7), the court reversed an order approving a debtor's petition under Chapter X, indicating that in view of the debtor's recent incorporation, pendency of a state court foreclosure suit and certain other facts and circumstances, there was an absence of the requisite good faith. Similar results were reached in *In re Williamsport Wire Rope Co.*, 10 F. Supp. 481, appeal dismissed 78 F. (2d) 1023 (C. C. A. 3) (petition under Section 77B dismissed for lack of good faith where plan did not appear feasible and continuation of existing equity receivership appeared more practical); *In re Philadelphia Rapid Transit Co.*, 8 F. Supp. 51, aff'd 73 F. (2d) 1022 (C. C. A. 3) (petition under Section 77B dismissed although literally within its terms, on the ground that good faith was lacking because petitioner's securities were acquired simply as means to institute the proceeding); *In re North Kenmore Bldg. Corporation*, 81 F. (2d) 656 (C. C. A. 7) (petition under 77B dismissed as not filed in good faith where debtor was incorporated in order to institute proceeding, had no equity in property and bondholders opposed); *In re Wisun & Golub, Inc.*, 84 F. (2d) 1 (C. C. A. 2). Cf. *In re Julius Roehrs Co.*, 115 F. (2d) 723 (C. C. A. 3).

Those judges of the Circuit Court of Appeals who have sat in the Second Circuit for the past nine years, are familiar with the proceedings which have been successfully conducted under the Schackno Act (Chapter 745 of the New York Laws of 1933, as amended) and under the Mort-

gage Commission Act (Chapter 19 of the New York Laws of 1935). When the guaranty mortgage companies defaulted on their guarantees early in 1933, there were approximately $700,000,000 of certificated mortgages outstanding. Immediately the Insurance Department, and subsequently the Mortgage Commission, was empowered under the above mentioned statutes to supervise the reorganization of these mortgages.* From the start and continuously during the past nine years the Second Circuit Court of Appeals has rejected efforts of various minority groups with doubtful motives to bring the administration of these mortgages into the federal courts. *Jacoby* v. *Bond & Mortgage Guarantee Co.*, 72 F. (2d) 420, cert. den. 293 U. S. 619; *Telfree* v. *New York Title & Mortgage Co.*, 72 F. (2d) 702, cert. den. 293 U. S. 619; *Depen* v. *Lawyers' Title & Guaranty Company*, 72 F. (2d) 705, cert. den. 293 U. S. 619; *Brooklyn Trust Co.* v. *Rembaugh*, 110 F. (2d) 838; *In re Blinrig Realty Corporation*, 114 F. (2d) 100; *In re Paloma Estates, Inc.*, decided February 21, 1942 (Judges Learned Hand, Chase and Clark) unreported. See also *In re Coney Island Hotel Corporation*, 76 F. (2d) 126; *In re Francfair, Inc.*, 13 F. Supp. 513 (S. D. N. Y.); *In re Reliable Estates*, 33 F. Supp. 588 (E. D. N. Y.). Cf. *Pennsylvania* v. *Williams*, 294 U. S. 176.

In *Brooklyn Trust Co.* v. *Rembaugh*, *In re Blinrig Realty Corporation* and *In re Paloma Estates, Inc.*, the court ordered dismissal of petitions under Chapter X be-

*For a history of the $700,000,000 of certificated mortgages so reorganized and placed under permanent trusteeships, see the report of the Mortgage Commission to His Excellency, the Honorable Herbert H. Lehman, Governor of the State of New York, and to the Legislature of the State of New York, dated April 1, 1939 (Legislative Document No. 94).

cause of pending Schackno reorganizations in the state court.

The record in the instant case is not appropriate to a determination, such as is apparently sought by the Securities and Exchange Commission, as to whether or not the jurisdiction of the state courts in all Schackno Act mortgage reorganizations should be ousted at the request of mortgagors and further "reorganization" of these mortgages maintained in the United States District Court for the Southern District of New York under Chapter X of the Bankruptcy Act. The Securities and Exchange Commission did not intervene until after the decision of the District Court, and when the case was in the District Court it was not known that efforts would be made to make it a test for determining the general question of jurisdiction between state and federal courts with respect to "Schackno mortgages". Therefore, some of the facts hereinafter set forth do not appear in the record. They are, however, matters of common knowledge to those engaged in the mortgage business in New York City, many of them appear in the reports of the Mortgage Commission to the Governor and the Legislature and in the annual reports of the Superintendent of Insurance to the Governor and the Legislature, and it has been deemed advisable that this Court, to assist it in determining whether or not certiorari should be granted in this case, should have such facts made available to it.

It is our information that in no state, except New York, and in almost no city, except New York City, were there companies which guaranteed certificated mortgages. It is our information that the reorganization of these guaranteed certificated mortgages is a problem which exists in New York State alone and largely in New York City alone. It

would seem to us therefore that there is no good reason why this court should be asked to review the decision of the Circuit Court of Appeals in this case. There is not, and in the nature of things there could not be, a conflict of circuits. The only question of federal law decided has been the procedure to be followed with respect to a problem peculiarly local and covered by a special set of state statutes.

The Second Circuit Court of Appeals has been aware of the fact that special terms have been created in the state courts and justices assigned to such terms whose chief function is the handling of these guaranteed certificated mortgages (R. 18-19; Chapter 19, New York Laws of 1935, Section 17a; Section 1768 of Unconsolidated Laws). It has also been aware of the fact that recently, by Chapter 704 of the Laws of 1940, amending Section 17a of Chapter 19 of the New York Laws of 1935 (The Mortgage Commission Act), the New York State Legislature has added still another cog to the comprehensive machinery of state court certificated mortgage reorganizations through the creation of an agency designated by the order of the Supreme Court, Kings County, as the Bureau of Trust Supervision. This bureau fulfills the functions formerly fulfilled by the Mortgage Commission, which has now gone out of existence. All applications for the further readjustment of certificated mortgages, where the property is located in the Second Judicial Department (as is this property), must be on notice to this bureau. It is the duty of this bureau to analyze each proposed plan of extension or liquidation, to appear in court and, with the benefit of the wide certificated mortgage reorganization experience which its personnel (who were formerly with the Mortgage Commission) have accumu-

lated over a period of years, to advise the court as to the fairness of the plan. It is the duty of the trustee to account annually to certificate holders and to the court (R. 27-28), and each such annual accounting is subject to the careful scrutiny of this bureau. Judge Frank, in his dissenting opinion (R. 118) emphasized the role played by the Securities and Exchange Commission in Chapter X proceedings, but it is respectfully submitted that the specialized experience which the Bureau of Trust Supervision has in dealing with certificated mortgages qualifies it to advise wisely in these matters far more than does the experience of the Securities and Exchange Commission, whose activities largely concern ordinary stocks and bonds.

Almost all of the certificated mortgages have been extended and modified and a trustee named under a standard declaration of trust similar to that appearing in this record. In the Second Judicial Department the services of leading trust companies in New York City have been enlisted and such companies uniformly have been named as trustees by the Kings County Supreme Court. Most of these certificated mortgages, formerly guaranteed by mortgage guaranty companies, were, like the instant mortgage, made in the late nineteen twenties or very early nineteen thirties and, as a result, most of them are today top-heavy, so that the property owners have no equity in the property. Most of the owners are "dummy" corporations, with no other asset than the mortgaged property, formed simply to avoid personal obligation on the mortgage bond. If each time one of these mortgages matures and the owner is unable to obtain the terms which it desires it is to be permitted to come into the federal court under the guise of a "reorganization" proceeding, it will be almost impossible successfully to consum-

mate the comprehensive scheme of economical and orderly liquidation created by and progressing under the state statutes.

Under the state court procedure property owners are required to pay the costs of mortgage extensions, which are small. If there is to be a Chapter X proceeding, the estate, which in reality is the mortgage certificates, must pay the trustee's fees, trustee's counsel fees, mortgage trustee's fees and fees of its counsel, possibly committee fees and expenses, possibly special master's fees, fees of debtor's attorneys, and the other expenses attendant upon a so-called "reorganization". (See Subchapter XIII of Chapter X; U. S. C., Sections 241, 242, 243).

The dissenting opinion (R. 113) suggests that a mortgage trustee appointed by a state court may have a selfish interest in continuing the state court proceeding, to wit: its fees. The standard declaration of trust limits its fees to one-twelfth of income distributed to certificate holders, not to exceed one-third of one percent per annum of principal. Its counsel ordinarily receive no fees from the trust (R. 29, 30). Moreover, upon default by a property owner, the standard practice is for the trustee immediately to institute foreclosure proceedings, convert the mortgage into real estate, sell the real estate and liquidate the trust upon notice to certificate holders and with court approval as soon as a good offer for the property is received. That is what the trustee is seeking to do here. Of course, upon liquidation, the fees of the trustee cease altogether.

It has been argued that perhaps some good to creditors —that is certificate holders—can result from a petition which has been filed by a debtor with no equity and which apparently is desired by no one other than the debtor. But

certificate holders have consented to the state court trusteeship by overwhelming vote. They have selected the trustee in their approval of the Schackno plan. Why should they be made to bear the expense of an attempted fictitious "reorganization" of a debtor who has no interest in the property? No one seriously expects the debtor to put in new money, since there is a deficit of $50,000 on the first mortgage alone, not to mention subordinate mortgages and conditional bills of sale.

It is said that perhaps a new corporation can be created to take over the property (R. 114). To organize a corporation and pay corporation taxes would be fruitless and far more expensive than the present trusteeship. The problem of converting numerous certificate holders into stockholders and enabling them to select directors who could and would operate the property honestly, expertly and efficiently is a difficult one. The so-called corporate method of "reorganizing" these certificated mortgages was tried in 1934, in the early days of the Shackno Act, and was rejected both by the certificate holders themselves and by the state courts as utterly unworkable and uneconomical. If certificate holders must terminate the mortgage because of the debtor's wilful default, what method is simpler and cheaper than to have the trustee conclude the foreclosure proceeding which has already proceeded for four and one-half months in the state court?

There has been a suggestion (dissenting opinion R. 123-124) that state court proceedings have sometimes been resorted to in order to avoid Chapter X proceedings. That claim, however, cannot be substantiated in the present situation where the New York State Legislature, Insurance Department, Mortgage Commission and courts have success-

fully and economically handled the entire certificated mortgage problem for almost nine years (Report of Mortgage Commission, *supra*, p. 10, n.

The danger which the trustee appointed by the state court faces in cases such a this is the possibility that the debtor, by consciously depreciating the value of certificates, will discourage certificate holders and cause them to sell their certificates in the over-the-counter market in New York City for far less than they are worth. In this way, a debtor may easily through brokers acquire most or all of the certificates, and thus the ownership of the mortgage itself, for far less than either its face or true value. In the instant case, that may well occur unless this proceeding is brought to a speedy halt. The debtor's wilful default in taxes and interest, although earnings of the property were then sufficient to cover such items (R. 16, 10), cut off the income of certificate holders. The necessary foreclosure proceeding, which followed has meant further delay in receipt by them of any income.* The debtor's president has stated in her affidavit that the price of the certificates in the open market on September 29, 1941 had dropped to 50% of "par" (R. 63). Unless the instant petition is denied there will be further expense, delay and absence of income to certificate holders with consequent further depreciation in the market value of certificates, all of which may well permit the debtor to benefit at the expense of needy certificate holders.

---

*Although a stipulation was recently signed, after hearing in the Circuit Court of Appeals, permitting the receiver to make repairs and pay taxes and interest, the receiver has asserted that under present circumstances, because of tax arrears, necessary repairs and the necessity of reserves to cover foreclosure expenses, he can make no interest payments.

CONCLUSION

It is respectfully submitted that the debtor-petitioner has shown no reason in law or in fact which would justify this Court in granting its petition for certiorari in this case and that therefore the petition should be dismissed.

Respectfully submitted,

HAROLD L. SMITH,
Attorney for Manufacturers Trust Company, Trustee.

CURTISS ELY FRANK,
Of Counsel.

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CHARLES ELMORE CROPLEY
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

No. ~~948~~ 24

MARINE HARBOR PROPERTIES, INC.,

Petitioner,

vs.

MANUFACTURERS TRUST COMPANY (successor by merger to The Mortgage Corporation of New York), as trustee for the benefit of certificate holders in mortgage guaranteed by Bond and Mortgage Guarantee Company, Guarantee #181,568,

MAURICE RUBINGER, trustee of Marine Harbor Properties, Inc.,

SAMUEL SILVERMAN, additional trustee of Marine Harbor Properties, Inc.,

MORTIMER RUBENSTEIN, Foreclosure-receiver,

and

SECURITIES AND EXCHANGE COMMISSION.

BRIEF OF MORTIMER RUBENSTEIN, FORECLOSURE RECEIVER

HAROLD STERN,
Attorney for Mortimer Rubenstein, Foreclosure Receiver.

GEORGE ROSLING,
Of Counsel.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

No. 948

MARINE HARBOR PROPERTIES, INC.,

Petitioner,

vs.

MANUFACTURERS TRUST COMPANY (successor by merger to The Mortgage Corporation of New York), as trustee for the benefit of certificate holders in mortgage guaranteed by Bond and Mortgage Guarantee Company, Guarantee #184,568,

MAURICE RUBINGER, trustee of Marine Harbor Properties, Inc.,

SAMUEL SILVERMAN, additional trustee of Marine Harbor Properties, Inc.,

MORTIMER RUBENSTEIN, Foreclosure-receiver,

and

SECURITIES AND EXCHANGE COMMISSION.

BRIEF OF MORTIMER RUBENSTEIN, FORECLOSURE RECEIVER

STATEMENT

Mortimer Rubenstein, the Receiver appointed in foreclosure proceedings in the State Court brought by the Manufacturers Trust Company, etc., as trustee, for the benefit of certificate holders, and one of the appellees below,

adopts and concurs in the position taken by Manufacturers Trust Company, as trustee, and rests upon the brief to be submitted by said Trust Company.

Dated, New York, March 9, 1942.

HAROLD STERN,
Attorney for Mortimer Rubenstein, Foreclosure Receiver.

GEORGE ROSLING,
Of Counsel.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1942.

No. 24

MARINE HARBOR PROPERTIES, INC.,
Petitioner,

against

MANUFACTURERS TRUST COMPANY (successor by merger to The Mortgage Corporation of New York), as trustee for the benefit of certificate holders in mortgage guaranteed by Bond and Mortgage Guarantee Company, Guarantee #181,568,
Respondent,

MAURICE RUBINGER, trustee of Marine Harbor Properties, Inc.,

SAMUEL SILVERMAN, additional trustee of Marine Harbor Properties, Inc.,

MORTIMER RUBENSTEIN, foreclosure-receiver,

and

SECURITIES AND EXCHANGE COMMISSION

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF OF RESPONDENT MANUFACTURERS TRUST COMPANY AS TRUSTEE

CHARLES E. HUGHES, JR.,
CURTISS E. FRANK,
Counsel for Respondent Manufacturers Trust Company, As Trustee.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1942

No. 24

MARINE HARBOR PROPERTIES, INC.,
Petitioner,

MANUFACTURERS TRUST COMPANY (successor by merger to The Mortgage Corporation of New York), as trustee for the benefit of certificate holders in mortgage guaranteed by Bond and Mortgage Guarantee Company, Guarantee #181,568,
Respondent,

MAURICE RUBINGER, trustee of Marine Harbor Properties, Inc.,

SAMUEL SILVERMAN, additional trustee of Marine Harbor Properties, Inc.,

MORTIMER RUBENSTEIN, foreclosure-receiver,
and

SECURITIES AND EXCHANGE COMMISSION.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF OF RESPONDENT MANUFACTURERS TRUST COMPANY AS TRUSTEE

Opinions Below

The opinion of the district court (Bright, *D. J.*) is contained in the record (R. 70-75) and is also reported in 41

F. Supp. 814. The majority (Swan, *C. J.* and Chase, *C. J.*) and dissenting (Frank, *C. J.*) opinions of the Circuit Court of Appeals are contained in the record (R. 107-126) and are also reported in 125 F. (2d) 296.

Jurisdiction

The jurisdiction of this court rests upon Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925.

Statutes Involved

Section 141 of Chapter X of the Bankruptcy Act (11 U. S. C. 541) provides:

> "§ 141. PETITION OF DEBTOR
>
> Upon the filing of a petition by a debtor, the judge shall enter an order approving the petition, if satisfied that it complies with the requirements of this chapter and has been filed in good faith, or dismissing it if not so satisfied."

Section 146 (11 U. S. C. 546) provides in part as follows:

> "§ 146. GOOD FAITH OF PETITION
>
> Without limiting the generality of the meaning of the term 'good faith', a petition shall be deemed not to be filed in good faith if—
>
> * * * * * * *
>
> (3) it is unreasonable to expect that a plan of reorganization can be effected; or
>
> (4) a prior proceeding is pending in any court and it appears that the interests of creditors and

stockholders would be best subserved in such prior proceeding."

Statement of the Case

Manufacturers Trust Company (successor by merger to The Mortgage Corporation of New York) is trustee for the benefit of certificate holders of a first mortgage in the present principal amount of $370,000 covering the land and apartment house building at 351-363 Marine Avenue, Brooklyn, New York, which is the debtor's sole asset* (R. 7). The debtor, a New York corporation formed by Abraham and Gussie Hammer, husband and wife, all of the stock of which is now owned by Gussie Hammer, acquired the real estate in February 1933 (R. 76, 95, 61, 8-9, 66).

The mortgage was executed in 1931 in favor of Title Guarantee and Trust Company, which sold participation certificates in the bond and mortgage to the general public. These participation certificates were guaranteed as to principal and interest by Bond and Mortgage Guarantee Company, which was taken over on August 2, 1933 for rehabilitation by the Superintendent of Insurance of the State of New York (R. 8). Pursuant to powers granted to him as rehabilitator of Bond and Mortgage Guarantee Company under Sections 3 and 4 of Chapter 745 of the New York

---

*The petitioner, in the opening sentence of its statement, refers to the apartment building as its "principal asset", but in paragraph 7 of its petition under Chapter X it swore "The debtor has no cash and no assets other than the property [apartment house] above referred to" (R. 82). The Securities and Exchange Commission has fallen into the same error in its statement (p. 4).

Laws of 1933 as amended (the Schackno Act), the Superintendent of Insurance on October 24, 1934 promulgated a plan for the readjustment, modification and reorganization of the rights of certificate holders in the mortgage, which plan provided for an extension of the mortgage indebtedness and a reduction of the interest rate thereon (R. 9).

The debtor entered into an agreement embodying the plan, appeared at the hearing on such plan in the Supreme Court, Kings County, by its then president Abraham Hammer, and consented in open court to the plan as modified by the court (R. 9, 49-51). Thereafter, more than 66⅔% of the holders in principal amount of certificates in such mortgage having consented to such plan as modified by the court, it became binding upon all parties in interest, including the debtor (R. 10, 53).

In 1938 the New York Mortgage Commission, by virtue of its powers under Chapter 19 of the New York Laws of 1935 (the Mortgage Commission Act), promulgated a further plan to modify the original plan promulgated by the Superintendent of Insurance to the extent of appointing a trustee of the bond and mortgage under an approved form of declaration of trust (R. 11). The debtor received notice of such plan and hearing thereon (R. 11). After hearing in the Supreme Court, Kings County, and upon the approval of more than 66⅔% in principal amount of certificate holders, a final order was entered on December 6, 1938 approving the plan and the form of declaration of trust and designating The Mortgage Corporation of New York as trustee (R. 11, 42).

In such final order, the Supreme Court, Kings County, retained jurisdiction of the proceedings through the following clause (R. 12, 44):

"ORDERED that this Court, having assumed jurisdiction of this proceeding, *shall retain jurisdiction hereof until the complete liquidation of the Trust Estate* and the termination of the trust; and the Trustee, or *any other interested party herein, may apply at the foot of this Final Order* upon such notice as the Court may direct *for such other and further relief as to the Court may seem just and proper.*"*

Pursuant to such final order, The Mortgage Corporation of New York duly qualified as trustee and the bond and mortgage were assigned to it by Title Guarantee and Trust Company and the Mortgage Commission (R. 12). Thereafter and until April 1941, when it defaulted in the payment of interest and taxes, the debtor made payments to the trustee in conformity with the final order approving the modified plan (R. 78-9).

Following the maturity of the mortgage on December 1, 1937, it ~~ran~~ "open" (R. 10, 8, 17). No principal amortization was required because of the New York Moratorium Laws (*New York Civil Practice Act, Sections 1077-a et seq.*). Earnings of approximately 6⅔% after taxes were more than sufficient to pay the mortgage interest of 5% (R. 16). The mortgage was exceedingly top-heavy. The principal amount of such mortgage, together with arrears of interest and taxes, was $384,931 on April 1, 1941, and $399,814.93 on October 1, 1941, while the value of the mortgaged premises did not exceed $350,000 (R. 15, 17, 56-57, 60, 71). Thus, entirely apart from the second, third and fourth mortgages and the balances due on conditional bills of sale, there was a deficit of approximately

*Italics in quotations in this brief are supplied unless otherwise noted.

$35,000 on April 1, 1941, and of approximately $50,000 on October 1, 1941. The debtor and the trustee had been negotiating on some plan which might prove feasible for further extension and modification of the mortgage (R. 14). The trustee took the position that in view of the top-heavy condition of the mortgage a fair plan would require the debtor to turn over substantially all of the earnings of the property to certificate holders. The debtor refused to meet such conditions (R. 14). Thereupon the debtor, instead of availing itself of the privilege of going into the state court which had retained jurisdiction of the matter, with a proposal for extension and modification of the mortgage, wilfully defaulted in the payment of interest and taxes despite the fact that earnings were sufficient to make such payments (R. 12, 16).

After the trustee's institution of the foreclosure action on May 1, 1941, the debtor further defaulted with respect to certain promises which it made for the clearing up of arrears and settlement of the foreclosure proceeding (R. 58-59). After the foreclosure action had proceeded for 4½ months with a state court receiver in possession, the debtor obtained an order *ex parte* approving its petition for "reorganization" under Chapter X (R. 96-101, 6).

Question Presented

The issue here is whether or not a mortgagor (debtor), whose only asset is a piece of improved real property encumbered by a certificated first mortgage greater in amount than the value of the mortgaged property, may force the first mortgagee into a Chapter X proceeding despite the fact that proceedings which are specially designed to safe-

guard the rights of the first mortgage certificate holders and in which the debtor has participated are pending in the state court.

Argument

The court, before approving a debtor's petition under Chapter X, must be "satisfied" that the "need for relief under this chapter" exists and that the petition has been filed in good faith in the general sense of that term as well as in the four specifically designated senses contained in the subdivisions of Section 146. (*Section 130, subdivision 7; Section 141; Section 146; 11 U. S. C. 530, subdivision 7, 541, 546*). The courts have often dismissed 77B and Chapter X proceedings under the general statutory provisions codifying their broad equity powers, when they have not believed that entertainment of the petition was warranted under existing circumstances. *In re North Kenmore Bldg. Corp.*, 81 F. (2d) 656 (C. C. A. 7th); *In re Wisun & Golub, Inc.*, 84 F. (2d) 1 (C. C. A. 2nd); *In re Philadelphia Rapid Transit Co.*, 8 F. Supp. 51, 55 (D. C., E. D. Pa.), aff'd 73 F. (2d) 1022; *In re Cook*, 104 F. (2d) 981, 985 (C. C. A. 7th); *In re Ware Metal Products*, 42 F. Supp. 538 (D. C., D. Mass.); see *Securities & Exch. Commission* v. *United States R. & Imp. Co.*, 310 U. S. 434, 455; *In re Julius Roehrs Co.*, 115 F. (2d) 723 (C. C. A. 3rd); *Finletter: The Law of Bankruptcy Reorganization* (1939), pages 73-85. In some instances, when the petition under Section 77B or Chapter X has been filed by a debtor, rather than by creditors who could have done so, the courts have dismissed the proceedings because of the personal disqualification of the debtor. *Brooklyn Trust Co. v. Rembaugh*, 110 F. (2d) 838, 840 (C. C. A. 2nd) (debtor

participated in prior state court proceedings); *In re Blinrig Realty Corporation*, 114 F. (2d) 100 (C. C. A. 2nd) (debtor participated in prior state court proceedings); *In re Wisun & Golub, Inc.*, 84 F. (2d) 1 (C. C. A. 2nd) (debtor concealed assets); *In re North Kenmore Bldg. Corporation*, 81 F. (2d) 656 (C. C. A. 7th) (debtor incorporated to file petition); *In re Francfair, Inc.*, 13 F. Supp. 513 (S. D. N. Y.) (debtor incorporated to file petition). See also *Shapiro* v. *Wilgus*, 287 U. S. 348. The very fact that a debtor, as petitioner in the instant case, although insolvent in the bankruptcy sense, is able to meet its current obligations as they mature may be sufficient reason for dismissal of its petition to "reorganize" under Chapter X. See *First Nat. Bank* v. *Flershem*, 290 U. S. 504, 516-519; *Finletter: The Law of Bankruptcy Reorganization* (1939), page 38: "* * * it is believed that few petitions [under Chapter X] will be granted on the basis of asset-liability insolvency unless the debtor is also unable to meet its current obligations."

The Securities and Exchange Commission Report of September 30, 1940, Part VIII, contains the following significant comments (pp. 94, 97):

> "In still other contexts, perhaps also reflecting no 'need for relief' under Section 77B, debtors' petitions were found lacking in 'good faith.' Thus, in instances where reorganization was near completion in pending equity receivership or foreclosure proceedings, courts refused to approve debtor's petitions which would have disrupted such proceedings. * * * In all these cases, it is apparent that the debtor's petition represented a last-ditch effort to salvage some interest which the equity proceeding would have denied to it; and the action of the courts

in these situations is further indication that Section 77B was not a mechanism for preserving equities at the expense of creditors. Rather, the 'need for relief' which a debtor was obliged to show was a need for the machinery of 77B as an essential in accomplishing a reorganization because other procedures were either unavailable or more cumbersome and expensive. In the cases cited, it was the debtor's inability to show this, other procedures having been successfully utilized, that led the courts to find an absence of 'good faith.'

* * * * * * *

[after citing further cases interpreting "good faith"]

These cases exemplify both the flexibility and the usefulness of the concept 'good faith' in connection with debtor's proceedings under Section 77B. Unquestionably its pliable character equipped the courts with a valuable power to sift and sort the cases with which they were presented.[67] In some respects, however, the power perhaps might have been utilized to a greater extent than the reported cases show."

"[67] In the revision of Section 77B contained in Chapter X of the amendatory Act, the flexibility of the provision is retained, while at the same time there is incorporated a codification of the interpretations given to it by the courts. Section 146 of the Act reads as follows: [quoting statute]."

Petitioner has the burden of establishing the need for relief under Chapter X and also its good faith in the general sense as well as in the four specific senses enumerated in the subdivisions of Section 146, and judicial approval of the petition should not be based solely upon the allegations of the petition but upon an independent

inquiry into the petitioner's good faith. *Manati Sugar Co.* v. *Mock*, 75 F. (2d) 284 (C. C. A. 2nd); *In re Cook*, 104 F. (2d) 981, 984 (C. C. A. 7th); *Hickey* v. *Ritz-Carlton Restaurant & Hotel Co.*, 96 F. (2d) 748, 751 (C. C. A. 3rd); *In re Grigsby-Grunow Co.*, 77 F. (2d) 200 (C. C. A. 7th); *Provident Mut. Life Ins. Co.* v. *University Ev. L. Church*, 90 F. (2d) 992, 995 (C. C. A. 9th); *In re Philadelphia Rapid Transit Co.*, 8 F. Supp. 51 (D. C., E. D. Pa.), aff'd 73 F. (2d) 1022. The mere *ex parte* approval of the petition by the district judge made upon a petition failing to disclose the terms of the state court order (R. 78, 80) can not cast the burden of proof upon respondent-trustee, and the cases cited by petitioner for that contention (its brief, p. 13) support rather than negative our view.

Since it is uncontroverted and the district court found (R. 70-71) that the indebtedness on the first mortgage is substantially greater in amount than the value of the mortgaged premises, the only proper subject of reorganization is the certificated mortgage which is already within the jurisdiction of the comprehensive procedure existing in the state courts. The case is therefore analogous to those cases in which this court and other federal courts have consistently ruled that, where there is a state statutory procedure available for the liquidation of corporations under the jurisdiction of state officers, the federal courts should relinquish jurisdiction "in favor of the statutory administration of the corporate assets by the state officer" in the absence of a showing by the party requesting the federal court to take jurisdiction that the interests of creditors and stockholders would not be adequately protected by the state court procedure. *Pennsylvania* v. *Williams*, 294 U. S. 176, 183; *Gordon* v. *Ominsky*, 294 U. S. 186; *U. S.* v. *Bank*

cf New York Co., 296 U. S. 463. Thus, in *Penn Co.* v. *Pennsylvania*, 294 U. S. 189, this court said (p. 197):

> "In the absence of a showing that the interests of creditors and shareholders would not be adequately protected by this procedure, the case was a proper one for the district court, in the exercise of judicial discretion, to relinquish the jurisdiction in favor of the administration by the state officer. See No. 394, *Pennsylvania* v. *Williams, supra.*"

It was in accordance with such principles that the majority of the Circuit Court of Appeals ruled: "That [the pending state court] proceeding provides adequate means to reorganize the mortgage and protect the rights of all certificate holders whose interests alone exhaust the debtor's property." (R. 110).

FIRST. The dismissal of the petition was correct, because prior proceedings are pending in which it appears that the interests of creditors and stockholders would be best subserved.

Preliminarily, it must be noted that while subdivision (4) of Section 146 mentions the interests of stockholders as well as of creditors, in the instant case, as was pointed out in both the majority and dissenting opinions of the Circuit Court of Appeals (R. 110, 115), under the doctrine of "absolute priorities" adhered to by this court, the interests of the first mortgage creditor need alone be considered. *Case* v. *Los Angeles Lumber Products Co.*, 308 U. S. 106; *Consolidated Rock Products Co.* v. *DuBois*, 312 U. S. 510.

A. The proceedings pending in the New York State Supreme Court are "prior proceedings" within the meaning of Section 146, subdivision (4).

Neither the dissenting opinion of the Circuit Court of Appeals (R. 113, 115-126), nor the opinion of the district court (R. 73-75), questioned the fact that the trust proceeding pending in the State Supreme Court was a "prior proceeding" within the meaning of Section 146, subdivision (4). But the debtor and the Securities and Exchange Commission now argue (*Petitioner's Brief*, pp. 11-13, 19-22; *Securities and Exchange Commission Brief*, p. 21) that these are not such prior proceedings, the former because the order appointing the trustee was a "final" order terminating "all prior proceedings in the state court for good and always" and because the debtor had "no standing in [the] Schaekno proceedings" (*Petitioner's Brief*, pp. 13, 22); and the latter because its concept of "prior proceedings" is that of a "proceeding in which the assets of a debtor were *in custodia legis* for the primary purpose of rehabiiitation or distribution for the benefit of claimants" (*Securities and Exchange Commission Brief*, p. 21, n. 21). None of these grounds is tenable.

That the state court proceeding was not terminated is shown by the order quoted *supra*, page 5. The argument of the Securities and Exchange Commission is not supported by the definition contained in the statute itself. But, apart from this and assuming *arguendo* that the argument might have some force if the debtor possessed other assets which would come into the custody of the federal reorganization court and which were not in the custody or under the jurisdiction of the state court, it is wholly unfounded where

as here the first mortgage, which completely exhausts the debtor's property, is under the jurisdiction of the state court both in the Schackno trust proceeding and in the foreclosure proceeding.

The language of subdivision (4) is broad; it is only required that "*a* prior proceeding" be pending, etc.; there is no requirement that the proceeding be of any particular type nor that the debtor shall have participated to any particular degree. In many instances where various types of state or federal "reorganization" proceedings have been pending, petitions under Chapter X and under Section 77B have been dismissed. *Tennessee Pub. Co.* v. *American Nat. Bank*, 299 U. S. 18, 21 (where district court had ruled "that it would 'manifestly be unjust to the bondholders' to undo what had been done in the equity case" and its order dismissing 77B petition was affirmed); *Brooklyn Trust Co.* v. *Rembaugh*, 110 F. (2d) 838 (C. C. A. 2nd) (Schackno Act trust proceeding pending in state court); *In re Bliirig Realty Corp.*, 114 F. (2d) 100 (C. C. A. 2nd) (Schackno Act trust proceeding pending in state court); *In re Paloma Estates, Inc.*, 126 F. (2d) 72 (C. C. A. 2nd) (Schackno Act trust proceeding pending in state court); *Price* v. *Spokane Silver & Lead Co.*, 97 F. (2d) 237 (C. C. A. 8th), cert. den. 305 U. S. 626 (state court receivership pending); *In re Williamsport Wire Rope Co.*, 10 F. Supp. 481 (D. C., M. D. Pa.), aff'd 78 F. (2d) 1023 (federal equity receivership pending); *In re Cook*, 104 F. (2d) 981 (C. C. A. 7th) (state court accounting suit pending); *In re Mallalieu & Conrey, Inc.*, 10 F. Supp. 808 (D. C., E. D. Pa.) (federal equity receivership pending); *In re Ashwood Realty Corp.*, N. Y. L. J., February 25, 1939; see 37 F. Supp. 670 (Schackno Act proceeding pending); *cf. Harkin* v. *Brundage*, 276 U. S. 36.

Moreover, the pendency of a state foreclosure proceeding has often been considered ground for dismissal of a petition under former Section 77B or under Chapter X, when the interest of the mortgagee conducting the foreclosure completely exhausts the property. *Wayne United Gas Co.* v. *Owens-Illinois Glass Co.*, 91 F. (2d) 827, 829 (C. C. A. 4th); *In re Suburban Properties*, 110 F. (2d) 438 (C. C. A. 7th); *Reighard* v. *Higgins Enterprises*, 90 F. (2d) 569 (C. C. A. 3rd); *In re Corn Kelly Corporation*, 32 F. Supp. 572 (D. C., E. D. N. Y.), aff'd 111 F. (2d) 644; *In re Francfair, Inc.*, 13 F. Supp. 513 (D. C., S. D. N. Y.). See also *Reading Hotel Corp.* v. *Protective Committee*, 89 F. (2d) 53 (C. C. A. 3rd), cert. den. 302 U. S. 742; *First Nat. Bank* v. *Conway Road Estates Co.*, 94 F. (2d) 736 (C. C. A. 8th), cert. den. 304 U. S. 578; *In re Murel Holding Corporation*, 75 F. (2d) 941 (C. C. A. 2nd).

The debtor's present argument that it has no standing in the state court is an afterthought. It never endeavored to assert any rights in the state court. If it had endeavored to proceed in the state court, it would have found that its right to do so is not open to question. *Wexford Realty Corp* v. *Manufacturers Trust Co.*, 263 App. Div. 971 (2nd Dept.) — appeal by owner-mortgagor; *Crane, Metro Estates, Inc., et al.* v. *Brooklyn Trust Co.*, 262 App. Div. 969 (2nd Dept.); *Feinstein, et al.* v. *The Mortgage Corporation of New York*, 264 App. Div. 783 (Mem.); *Plan 3521, Kings County Clerk's No. BMC 185,359, Premises 494 Sheffield Avenue, Brooklyn, New York*—after denial of extension application made by trustee, owner moved for reargument and application was granted; *Plan 2956, Kings County Clerk's No. BMC 180,865, Premises 301—81st Street, Brooklyn, New York*—owner moved, at the foot

of "final order" apprpving plan and appointing trustee, to alter plan with respect to tax payments and motion was granted; *Plan L-25, Kings County Clerk's No. BMC 181,338, Premises 1539 Bergen Street, Brooklyn, New York; Plan 1602, Kings County Clerk's No. LMG 29,159, Premises 292 to 304 Midwood Street, Brooklyn, New York; Plan 2073, Kings County Clerk's No. BMC 170,884, Premises 5619—15th Avenue, Brooklyn, New York; Plan 48-M, Kings County Clerk's No. BMC 181,010, Premises West Side of First Avenue, between north side of 58th Street and south side of 57th Street, Brooklyn, New York; Plan 202-M, Kings County Clerk's No. BMC 180,677, Premises 162-04 Jamaica Avenue, Jamaica, Queens, New York; Plan 811-M, Kings County Clerk's No. BMC 215,572, Premises 325 Bowery, Manhattan, New York; Plan 5164, Kings County Clerk's No. LMG 200,152, Premises 353 to 347 Fourth Street, Brooklyn, New York; Plan 4612, Kings County Clerk's No. LTG 257,444, Premises 99 Ocean Avenue, Brooklyn, New York;* see also *Matter of Bond & Mortgage Guarantee Company (Paragon Land Corporation; Joseph P. Day)*, 288 N. Y. 270.

B. The pending proceedings in the state court will best subserve the interests of creditors*.

It must be emphasized at the outset that this is not the case of a debtor corporation with a complicated financial

*The suggestion in the brief of the Securities and Exchange Commission (p. 4) that its presentation of the case "has been broadened" because of our statement in our letter dated March 28, 1942 written to the clerk of this court, is surprising. The complete sentence from which the brief quotes was:

"In view of the intervention of the Securities & Exchange Commission *and the position taken by it in its*

structure engaged in a business involving the creation and maintenance of good will, in which event its creditors and stockholders would probably benefit from the elaborate mechanism prescribed by Chapter X and explained in detail

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> *memorandum in support of the petition for writ of certiorari*, this case is generally regarded as involving a test as to whether approximately $700,000,000 in principal amount of certificated mortgages covering real estate in New York City and immediately adjoining counties will be reorganized under a procedure established by the New York Legislature or pursuant to the procedure provided in Chapter X of the National Bankruptcy Act."

In the memorandum referred to, the Securities and Exchange Commission indicated for the first time that it considered this case a test case, stating in such memorandum (pp. 12-13):

> "5. The importance of the issue involved in this case is manifest. Thousands of certificated mortgage issues are being 'reorganized' in the state courts, and many of these 'reorganizations' have taken the form, as in the present case, of a short extension of the maturity of the mortgage. As these extensions expire, further 'reorganization' is needed. The decision in the present case will, to a large extent, determine whether the federal procedure provided by Chapter X shall be available for such further reorganization."

The Securities and Exchange Commission did not intervene in this proceeding until after the decision of the district court, and when the case was in the district court it was not known that efforts would be made to make it a test for determining generally the question of jurisdiction between state and federal courts with respect to "Schackno mortgages".

While we believe that the burden of showing the advantages of a Chandler Act proceeding over a continuation of the proceedings in the state court rests upon petitioner, we shall, for the information of the court, present herewith certain material contained in public documents compiled during the course of ten years of state certificated mortgage reorganizations, which we believe demonstrates conclusively that at least in this case the interests of creditors will be best subserved by a dismissal of this petition and a continuation of the proceedings in the state court.

in the dissenting opinion (R. 116-123). This is the case of a debtor corporation owned by one person and formed to hold a single piece of real property, its only asset, the value of which is far exceeded by the amount of its first mortgage indebtedness.

The first mortgage has been permanently reorganized pursuant to a statutory scheme, worked out by the New York authorities after several years of study, by the appointment of a trustee under an approved uniform form of declaration of trust. *Annual Report of the Mortgage Commission dated April 1, 1939, N. Y. Legislative Document (1939) No. 94.* From May 1, 1935 to March 31, 1939, 13,511 certificated mortgages in the aggregate principal amount of $583,060,045 had been reorganized in the State Supreme Court pursuant to the Schackno Act or Mortgage Commission Act*, for the most part by the appointment or election of permanent trustees acting under the standard form of declaration of trust.** From September 1933 to

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*Debtor-petitioner is incorrect in its statement that Schackno proceedings were instituted "to rehabilitate or liquidate various bond and mortgage companies that had become insolvent and defunct" (*Petitioner's Brief*, p. 6). In reality, those Acts, by their very terms, were designed primarily to provide a vehicle for the permanent reorganization of the rights of certificate holders in particular mortgages or groups of mortgages.

**This form of declaration of trust was devised after many consultations between the courts handling certificated mortgage matters, the Mortgage Commission, the Insurance Department and attorneys specializing in this field and representing certificate holders (*Report of the Bureau of Trust Supervision*, p. 7, see *infra*, p. 20; *Matter of New York Title and Mortgage Co. (Series F-1)*, 160 Misc. 283). Although there were slight differences between the forms employed in some of the various counties of the metropolitan area, these differences are of no materiality here. *Report of June 18, 1936 of the Securities and Exchange Commission*, p. 185, n. 1, see *infra* p. 18.

May 1, 1935, $324,850,161.59 principal amount of certificated mortgages, involving over 100,000 investors, had been partially or fully reorganized in the same manner. *The Administration of the Delinquent Title and Mortgage Guaranty Companies by the New York Insurance Department, a Survey by George S. Van Schaick, Superintendent of Insurance, dated May 10, 1935*, p. 43; *Annual Report of the Mortgage Commission dated April 1, 1939, supra*, p. 17.

In the report of June 18, 1936 of the Securities and Exchange Commission on the Study and Investigation of Reorganization Committees, which study and investigation was headed by Mr. (now Mr. Justice) William O. Douglas, it is stated (Part VI, p. 185):

> "An unusually active type of trusteeship exists in New York State, in connection with the reorganization of issues of guaranteed mortgage certificates. Under the standardized form of declaration of trust, used with only minor modifications in dozens of these reorganizations, the trustee purports to be under a higher standard of obligation to the security holders than trustees under other indentures. Furthermore, he has express authorization to perform a broad range of acts looking toward future reorganization. This type of trusteeship has developed out of a situation of unique complexity and peculiar difficulty. However, many features of the trusteeship itself seem to have no inherent restriction either to the type of security or the type of procedure wherein it originated, and it is therefore a suggestive analogy for other trusteeships, particularly in the field of real estate securities."

This trust instrument, set forth at length in the record at pages 22-37, which was adopted with the consent of more than two-thirds in principal amount of the certificate

holders* and the approval of the court (R. 11, 42), is admirably adapted to the purpose for which it was created. Under it, the trustee is given broad powers and at the same time large responsibility in the handling of the certificated mortgage. The trustee must account annually (R. 27; *McKinney's Unconsolidated Laws*, Section 4815). It cannot extend or modify the bond and mortgage of which it is trustee nor sell the underlying property in the event of foreclosure without the permission of the court obtained "in said reorganization proceeding" after notice by mail to certificate holders. The trust is under the supervision of the Supreme Court, Kings County, where Mr. Justice George E. Brower, designated by the Appellate Division, Second Judicial Department, to preside over all certificated mortgage matters, has passed upon all such matters for almost ten years. *McKinney's Unconsolidated Laws*, Section 4819; *Order of the Appellate Division designating additional special term, New York Law Journal, July 31, 1933; The Administration of the Delinquent Title and Mortgage Guaranty Companies, supra*, p. 16; *Report of the Bureau of Trust Supervision, infra.*

By Chapter 704 of the Laws of 1940, the legislature authorized the creation of the Bureau of Trust Supervision. It, in effect, was to supersede the Mortgage Commission, which had then gone out of existence, in the performance of advisory services to the courts supervising certificated mortgage matters. Its excellent work through experienced personnel in advising the court on annual ac-

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*The statement in petitioner's brief (p. 17), that certificate holders were "against their will * * * dragged into the State Schackno proceedings", is, to say the least, misleading, as is the conclusion of the dissenting opinion (R. 125).

counts, on extensions and modifications of mortgages, on sales of foreclosed properties and in other related matters, is set forth in detail in its report to the Justice presiding over certificated mortgage matters in the Second Judicial District, entitled *Report of the Bureau of Trust Supervision to the Justice Presiding at Special Terms for the Reorganization of Guaranteed Certificated Mortgages in the Second Judicial District*, filed in the office of the Clerk of Kings County, #5791/1940. Upon the argument, copies of such report will be made available to the Court for its information, so the contents thereof will not be discussed in detail here.

As indicated in the Bureau's report, the trustee, normally (as in this case, R. 20) endeavors to obtain an extension and modification of the mortgage upon terms assuring to certificate holders substantially all of the income which the property yields unless the owner has an equity in the property entitling it to a share of the income.*

If terms can be agreed upon which are satisfactory to the court and certificate holders, an extension and modification agreement is entered into between the trustee and the debtor after a hearing upon notice to certificate holders in which the Bureau of Trust Supervision participates. Full information as to the appraised value of the property, its assessed value, its physical condition, neighborhood conditions, and earnings of the property, as checked by the trustee's auditors and appraisers and by the Bureau of Trust

*It should be noted that certificate holders for the most part acquired their certificates by paying par for them before the collapse of the mortgage guaranty companies in 1932, while property owners often, as is apparently the fact in this case, acquired their "equities" as a speculation during the depression (R. 8; see Chapter 745, N. Y. Laws of 1933; Chapter 19, N. Y. Laws of 1935).

Supervision, is furnished to certificate holders and the court (*Report of the Bureau of Trust Supervision, supra*, p. 15). All expenses of such proceeding are paid by the debtor, except for a nominal charge of the Bureau of Trust Supervision, which is paid out of the trust (*Report of the Bureau of Trust Supervision, supra*, pp. 6, 15, 9 [footnote]). The declaration of trust limits the trustee's fees to the commissions therein specified and permits no fees to attorneys except in the unusual event of actual legal proceedings, in which event they are subject to court approval (R. 29-30).

If a fair extension and modification arrangement cannot be worked out with the property owner* and the situation is hopeless, a foreclosure or taking of a deed in lieu of foreclosure from the owner are the only alternatives. In case of a deed in lieu of foreclosure, title is ordinarily

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*The Securities and Exchange Commission contends (its brief, pp. 24-25) that the state procedure is inadequate, because it provides for "short extensions of the mortgages" without requiring "payment" or "refunding". Of course, the term of the extension is within the discretion of the state court and depends upon the circumstances of the particular case (R. 26). If it is feasible to refinance the mortgage and liquidate it by full or adequate partial payment to certificate holders, such a plan also can be presented to the state court (R. 26). In many cases, where the debtor has sufficient equity to permit a refinancing, liquidation has been accomplished in this manner (*Report of Bureau of Trust Supervision, supra*, pp. 12-14). The state court follows the doctrine of absolute priorities enunciated by this court, *Chase Nat. Bank* v. *10 E. 40th St. Corp.*, 238 App. Div. 370 (1st Dep't); *Clinton Trust Co.* v. *142-144 Joralemon Street Corp.*, 237 App. Div. 789 (2nd Dep't); 49 Yale Law Journal 1443, 1455, and will not permit a debtor who has no equity, as in the instant case, to formulate a liquidation plan which will take anything away from the senior claimants, the certificate holders, whose interests exhaust the debtor's property. Therefore, in cases like the present, relatively short extensions of the mortgage or foreclosure are the only feasible alternatives.

obtained in a few days with practically no expense; in case the owner will not voluntarily execute a deed or subordinate liens must be cut off and foreclosure is necessary, title is ordinarily obtained by the trustee within a period of from three to five months. Foreclosure fees and expenses are passed upon by the court (*Report of the Bureau of Trust Supervision, supra,* p. 9). Since the trust is specifically a liquidating trust (R. 30-31), the trustee endeavors to dispose of the premises to which it has thus acquired title as soon as a reasonable offer can be obtained. In many instances, the trustee takes back a purchase money mortgage for part of the purchase price from the purchaser of the premises and in such instances the purchase money mortgage becomes a part of the trust estate (*Report of the Bureau of Trust Supervision, supra,* p. 13). We do not presume it will be argued that Messrs. Rubinger and Silverman, the trustees appointed by the District Court, could more effectively sell the mortgaged premises than could Manufacturers Trust Company with its large experience in real estate matters and expert personnel (see *Report of the Bureau of Trust Supervision,* pp. 7, 16, 18).

When foreclosure becomes necessary or title is taken through a deed in lieu of foreclosure and repairs have to be made and taxes and insurance premiums paid, the trustee often has to advance substantial sums* of its own money for such purposes, which of course are recouped whenever possible out of the proceeds of the trust properties (*Report*

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*According to the report of the Bureau of Trust Supervision as of December 31, 1941, the corporate trustees in the Second Judicial District had advances outstanding made from their own corporate funds to the various trust estates for the purpose of paying taxes, insurance, disbursements, etc. of $1,067,532.65.

of the Bureau of Trust Supervision, supra, p. 19; R. 25-27, Articles II, V).

As against this inexpensive, efficient and simple procedure which in every way completely protects the certificate holders whose interests alone need to be considered in this case, the debtor and the Securities and Exchange Commission endeavor to set the so-called "safeguards" of a Chapter X proceeding. These might well be valuable in a proceeding involving an industrial corporation with several outstanding issues of stocks and bonds, but they are not at all applicable in this instance.

The debtor argues that under a Chapter X proceeding foreclosure would not be necessary (*Petitioner's Brief,* 7) for the acquisition of title, and the dissent in the Circuit Court of Appeals argues that a plan can be effected whereby "without the expense or delay involved in foreclosure, the property will promptly be turned over to a new company, having no debts, all of the stock being ratably distributed among the certificate-holders" (R. 114). This is the so-called corporate method of reorganization, which was tried in the state courts some years ago and found wanting. *The Administration of the Delinquent Title and Mortgage Guaranty Companies, supra,* pp. 39-40; *Report of George W. Alger, Commissioner, to His Excellency Herbert H. Lehman, Governor of the State of New York, dated October 5, 1934,* p. 77. To organize a corporation and pay corporation taxes would be fruitless and far more expensive than the present trusteeship. There would be no protection by the court for certificate holders after the corporation was once launched. The problem of converting numerous certificate holders into stockholders and enabling them to select

directors who could and would operate the property honestly, expertly and efficiently is a difficult one. The establishment of a fiduciary relationship with a trained responsible trustee and the retention of supervision by the court has been found to be superior to any other method. *Matter of New York Title & Mortgage Co.*, 153 Misc. 858, 864-866; see also *Matter of New York Title & Mortgage Co.*, 154 Misc. 447; *Matter of Lawyers Mortgage Co.*, 277 N. Y. 244. If certificate holders must terminate the mortgage because of the debtor's wilful default, what method is simpler and cheaper than to have the trustee conclude the foreclosure proceeding which has already proceeded for 4½ months in the state court?*

It is further argued that a Schackno trustee is not "able to cope with a debtor's fraud or dishonesty", and that the Schackno trustee does not "possess power to investigate and probe the debtor as to its past management or its future prospects" (*Petitioner's Brief*, p. 7). But *Weil, et al.* v. *President and Directors of Manhattan Company*, 275 N. Y. 238, cited by petitioner, merely held that a Schackno trustee was not vested with the right to prosecute claims, owned by

*The Securities and Exchange Commission argues (its brief p. 26) "that the foreclosure must either end in a forced sale * * * or it must serve as the procedural vehicle for a reorganization according to the well-known pattern of equity receiverships", and that "it was this very type of inadequate equity procedure which Chapter X" was designed to supplant. The Commission misapprehends the simple procedure followed in New York State upon the foreclosure of an ordinary real estate mortgage. As hereinbefore explained, there is no involved judicial reorganization, nor is there any "forced sale"; there is simply the acquisition of legal title by the Schackno trustee through its usually nominal bid at the foreclosure sale, the property thereupon becoming the corpus of the trust.

individual certificate holders, for past breaches of trust by a depositary. It did not hold that *class* claims belonging to all certificate holders were not vested in a Schackno trustee. Such claims, which would include any action brought for the benefit of all certificate holders predicated upon the debtor's fraud or dishonesty, would, by the very terms of the declaration of trust, be vested in the Schackno trustee (R. 24). See *Matter of People* (*Lawyers Westchester Mortgage and Title Company*), 288 N. Y. 40. This, however, is academic in the present case, as it would be in most Schackno trust cases, because the debtor is a mere shell, hopelessly insolvent, with no asset other than this apartment house (R. 82). There is no reason to believe that a right of action against corporations holding mortgaged premises in cases of this type is of any value.

The debtor (*Petitioner's Brief,* p. 14) and the dissenting opinion in the Circuit Court of Appeals (R. 113) argue that the respondent may be motivated by selfish interests in seeking to have "the state court proceeding continue, because the trustee derived emoluments therefrom which would terminate if the Chapter X proceeding was not dismissed" (R. 113). During the period in which the trustee holds the title to real estate as a result of a property owner's default, its operations will not be as profitable as they would be if it were holding the mortgage, because, although it may retain a managing agent on a commission basis as set forth in the declaration of trust (R. 30), its duties and responsibilities in managing the real estate are considerably increased. As soon as the property is sold, the fees of the trustee cease altogether. The trustee is simply performing its duty to the state court which appointed it to assert its custody over the *res. In re Heilbroner,* 69 F.

(2d) 643, 644 (C. C. A. 2nd); *Bryan v. Speakman*, 53 F. (2d) 463 (C. C. A. 5th), cert. den., 285 U. S. 539. The reason this cause is in this court is because the trustee, in zealously insisting that the rights of certificate holders be protected to the extent of refusing to approve an extension agreement the terms of which were believed by it to be inadequate, has precipitated a foreclosure which may well result in a complete liquidation and termination of the trust and cessation of its fees. It should also be noted that respondent's trusteeship will not necessarily terminate under a Chapter X proceeding, so that its only motive in opposing this proceeding is a protection of the rights of certificate holders.

There has been a suggestion (Dissenting Opinion, R. 123-124) that state court proceedings have sometimes been resorted to in order to avoid Chapter X proceedings.* That assertion, however, cannot be substantiated in the present situation, where the New York State Legislature, Insurance Department, Mortgage Commission and courts have sucessfully and economically handled the entire certificated mortgage problem for almost nine years (*Report of the Bureau of Trust Supervision, supra* pp. 5-7; *Annual Report of the Mortgage Commission dated April 1, 1939, supra; Reports of Joint Legislative Committee to Investigate The Guaranteed Mortgage Situation, Legislative Documents (1934) Nos. 120 and 121; Report of George W. Alger, Commissioner, to the Governor, supra*, pp. 77-78).

The comments of Mr. (now Mr. Justice) William O. Douglas, in considering the relative desirability of federal

*The only authority for this suggestion cited by the dissenting opinion is a statement made in a note by the editors of the New York University Law Quarterly, XVIII N. Y. U. Law Quarterly Review, 399, 415, 417.

or state control over wage earner bankruptcies, are pertinent. In concluding that essentially local problems should be permitted to be handled by the states themselves, he said:

> "It seems desirable * * * to utilize to the fullest possible extent the administrative procedures and techniques which states have evolved or with which they have gained experience. The alternative of raising a new and huge federal superstructure to handle a function of some familiarity and experience in the states seems unwise." Douglas, Wage Earner Bankruptcies—State vs. Federal Control (1933), 42 Yale L. J. 591, 637-8.

It has been argued by petitioner, the Securities and Exchange Commission and the dissenting opinion that perhaps some good to creditors—that is certificate holders—can result from a petition which has been filed by a debtor with no equity and which apparently is desired by no one other than the debtor. But certificate holders have consented to the state court trusteeship by overwhelming vote. They have selected the trustee in their approval of the Schackno plan. Why should they be made to bear the expense of an attempted fictitious "reorganization" of a debtor which has no interest in the property? Under the state court procedure, as above stated, property owners are required to pay the costs of mortgage extensions, which are small. If there is to be a Chapter X proceeding, the estate, which in reality is the mortgage certificates, must pay the trustee's fees, trustee's counsel fees, debtor's counsel fees, mortgage trustee's fees and fees of its counsel, possibly committee fees and expenses, appraiser's fees, possibly special master's fees, the fees of any persons who assist in working out a plan of reorganization and the other expenses attendant

upon a so-called "reorganization". See Subchapter XIII of Chapter X; 11 U. S. C. 641, 642, 643.

In *In re Frank Realty Co.*, 31 F. Supp. 816 (D. C., M. D. Pa.), the trustee in a Chapter X proceeding disclaimed the debtor's three mortgaged properties because there was no equity in them for the debtor, but the court held that all expenses of the Chapter X proceeding, including appraiser's fees, advertising expenses, special master's fees and trustee's fees and expenses, must be assessed against the mortgagees.

In Schackno trusteeships in the Second Judicial District, the only expense to the trust estates of "reorganizations" consisting of the extension and modification of mortgages has been the costs of the Bureau of Trust Supervision, and the entire cost of operating such Bureau has averaged approximately .011614 of one per cent. per annum of the principal amount of the trusts (*Report of the Bureau of Trust Supervision, supra*, p. 19, footnote p. 9). On the other hand, the expense of federal equity receivership proceedings and of 77B proceedings in the Southern District of New York has been notoriously high, and for the period July 1, 1928 through June 30, 1939 the fees and expenses of administration in bankruptcy proceedings in that district averaged approximately 30% of the assets realized in the bankruptcy estates. 49 Yale Law Journal, p. 9; *House Report No. 3012, 74th Cong. 2d Sess. (1936)*. In the latter report (page 4), it is stated: "Moreover, enactment of the law [H. R. 12064 (An act to amend the Bankruptcy Act of July 1, 1898, to prevent loss of assets and excesive charges in connection with certain reorganizations, compositions, and extensions, * * *)] will eliminate the tremendous and exorbitant costs and fees which have been taken out of the assets in reorganization proceedings under sections 74 and 77B, and there will be no

additional expense to the Federal Government by the designation of the Comptroller of the Currency as Conservator." There is every reason to believe that Chapter X proceedings, because of their further complexity resulting from the additional safeguards they attempt to provide, will prove more costly than have 77B proceedings. *House Hearings on Chapter X*, pp. 367-368 (Sen. Doc. No. 1916, Part 2, 75th Cong., 3d Sess. [1938]6); 52 Harvard Law Review 1349, 1350.

In the one case in which the Circuit Court of Appeals has permitted a Schackno mortgage to be reorganized under Chapter X, *In re Castle Beach Apartments*, 113 F. (2d) 762 (C. C. A. 2nd), the mortgage was in the principal face amount of $441,250, the applications for allowances totalled $35,608.27 and the allowances awarded, exclusive of trustee's administration expenses of $958.37, totalled $11,354.52 (S. D. N. Y. #75836).

The legislative committee appointed to investigate the reorganization of certificated mortgages in New York, in comparing reorganizations effected under the Mortgage Commission and Schackno Acts with those effected under Section 77B with respect to the Prudence Company (which was not an insurance company and whose "bond issues" were not subject to the Mortgage Commission or Schackno Acts), concluded (*New York Legislative Document* [*1938*] *No. 87*, p. 17):

> "Furthermore, in a reorganization under section 77B, the proceedings were complicated and became extended over a long period of time. In such proceedings applications for allowances and fees were made by attorneys for the debtor, numerous certificate holders committees, special masters, trustees, attorneys for trustees, and numerous others, some

of whom had taken insignificant parts in the proceedings. In a number of instances, allowances were made to many of the applicants, creating a burden upon the certificate holders, who eventually were required to pay the cost thereof. *Most of the reorganization proceedings provided merely for the extension of the principal, reductions of the interest rate and the adjustment of arrears.*

In order to remedy the foregoing condition, your committee recommends that the Mortgage Commission Act be amended (Chapter 19 of the Laws of 1935) so that the Mortgage Commission may institute a reorganization proceeding involving a certificated mortgage issue guaranteed by a corporation other than one under the jurisdiction of the Superintendent of Banks or of the Superintendent of Insurance. The latter reorganization proceeding is speedy, expeditious and comparatively inexpensive."

It is interesting to note that in the very recent case of *In the Matter of Jacksonville Gas Company and American Gas & Power Company* (U. S. D. C., S. D. Fla.), decided September 22, 1942, the Securities and Exchange Commission, acting under the Public Utility Holding Company Act of 1935 [15 U. S. C. 79k(e)], promulgated and obtained court approval for enforcement of a plan of reorganization of a utility company providing for the acquisition of title to its property by prior creditors whose interests exhausted the debtor's property, without the expensive and lengthy procedure of Chapter X. In that connection, *The New York Times, September 27, 1942,* Section 3, p. F1, col. 8, reports:

"'There is no reason,' a high source at the SEC said today, 'that I can see why the same formula

could not be made available to any company finding itself in a situation not unlike that of Jacksonville Gas.

"The stresses and strains imposed by the war upon non-war industries most certainly are producing and will continue to produce just such situations. As compared with 77B and Chapter X of the Bankruptcy Act, with their long, costly and involved litigations, we submit that the Jacksonville plan, handled by personnel selected specifically for their task, could achieve better results in less time and with much less expense."

In addition to the expense item, there are other positive disadvantages of a federal court proceeding. In a group issue, such as exists in *In re Paloma Estates,* 126 F. (2d) 72 (C. C. A. 2nd), cert. filed May 12, 1942, No. 89 this term, where there are 102 mortgages and properties held by a trustee for the benefit of 7,500 certificate holders, (each holder having an aliquot interest in each of the 102 mortgages and properties), the reorganization of any one of such mortgages under a Chapter X proceeding means, under the view of the law held by petitioner, that all 7,500 of the certificate holders must be parties to the proceeding and the expense of several printings and mailings alone will be enormous. All of the remainder of the mortgages will still be subject to the jurisdiction of the state court and to the action of the trustee in that court, so that there will be needless duplication and overlapping of effort, together with much confusion.

Moreover, the Schackno trustees have been authorized to and have filed blanket claims against the guaranty companies on behalf of certificate holders and these claims are now being adjusted through the intermediation of the trus-

tees and dividends thereon are being paid to certificate holders through them. *Matter of People (Lawyers Westchester Mortgage and Title Company)*, 288 N. Y. 40. Also, at the present time allocation proceedings are pending in the state courts to fix the costs of the Superintendent of Insurance and of the Mortgage Commission during the periods that they serviced the mortgages and the Schackno trustees are parties to such proceedings. See *In re Pink*, 34 N. Y. Supp. (2d) 758 (Sup. Ct.) (interlocutory order confirming allocation of expenses of Mortgage Commission).

Individual trustees appointed in the federal court will have no familiarity with these matters and probably no power to represent certificate holders with respect to them. This will mean that the Schackno Act trustees will have to continue to function in some matters while the Chandler Act trustees will have to function with respect to other matters. Furthermore, there is the danger that the guaranty of the guaranty companies may be released, at least when the guaranty company is still in rehabilitation, by the consummation of a proceeding under the Chandler Act modifying the rights of certificate holders. The Schackno Act specifically provides that the liability of guaranty corporations with respect to mortgage investments guaranteed by them shall not be discharged by any action taken pursuant to that Act (*Laws of 1933, Chapter 745, Section 7; McKinney's Unconsolidated Laws*, Section 4878). There is no similar provision in Chapter X.

With this background, it is readily understandable why the District Court judges who have sat in the Southern District of New York, and the Circuit Court judges who have sat in the Second Circuit, for the past ten years, have almost uniformly rejected efforts of various minority

groups with doubtful motives to bring the administration of Schackno mortgages into the federal courts. *Jacoby* v. *Bond & Mortgage Guarantee Co.*, 72 F. (2d) 420 (C. C. A. 2nd), cert. den., 293 U. S. 619; *Tolfree* v. *New York Title & Mortgage Co.*, 72 F. (2d) 702 (C. C. A. 2nd), cert. denied, 293 U. S. 619; *Depen* v. *Lawyers' Title & Guaranty Company*, 72 F. (2d) 705 (C. C. A. 2nd), cert. den., 293 U. S. 619; *Brooklyn Trust Co.* v. *Rembaugh*, 110 F. (2d) 838 (C. C. A. 2nd); *In re Blinrig Realty Corporation*, 114 F. (2d) 100 (C. C. A. 2nd); *In re Paloma Estates*, 126 F. (2d) 72 (C. C. A. 2nd). See also *In re Coney Island Hotel Corporation*, 76 F. (2d) 126 (C. C. A. 2nd); *In re Francfair, Inc.*, 13 F. Supp. 513 (D. C., S. D. N. Y.); *In re Reliable Estates*, 33 F. Supp. 588 (D. C., E. D. N. Y.).

From an inspection of the files of the United States District Courts for the Southern and Eastern Districts of New York, it appears that only five guaranteed certificated mortgages subject to the comprehensive state legislation hereinbefore mentioned have been reorganized in the district court and in but one case was this done after the appointment of a Schackno trustee.* This may be contrasted with

*Of eighteen guaranteed certificated mortgage proceedings arising under Section 77B in the Southern and Eastern Districts, where no Schackno trustee had been appointed, eleven were dismissed at the outset, three were retained by the federal courts but later dismissed and remitted to the state courts where permanent trustees were appointed, one was reorganized in the federal court but on expiration of the extension was remitted to the state court where a permanent trustee was appointed, and only three were finally reorganized in the federal courts. Those dismissed at the outset were: *In re Avrum Realty Co.* (S. D. N. Y. #61,228); *In re Bailey Realty Co.* (S. D. N. Y. #61,831); *In re Bedford Realty Co., Inc.* (S. D. N. Y. #60,420); *In re Clarose Holding Corp.* (E. D. N. Y. #27,674); *In re Duce Realty Corp.* (E. D. N. Y. #27,928); *In re Sorola Holding Corp.* (E. D. N. Y.

the fact that well over 13,511 guaranteed certificated mortgages have been reorganized in the State Supreme Court (*supra*, p. 17).

#27,904); *In re 25 East 77th Street Co.* (S. D. N. Y. #60,978); *In re Francfair*, 13 F. Supp. 513 (D. C., S. D. N. Y.); *In re Truesdale Lake Corp.* (S. D. N. Y. #62,215); *In re 24th Street Studio Building Corp.* (S. D. N. Y. #61,556); *In re Walter-arms Realty Co.* (S. D. N. Y. #60,924). The three retained by the federal court and later remitted to the state court were: *In re Church E. Gates & Co.*, 97 F. (2d) 911 (C. C. A. 2nd)—order of dismissal signed June 27, 1939 (S. D. N. Y. #69,680)—order appointing trustee signed June 29, 1939 (Supreme Court, Bronx County, #5,822/1937, *sub nom. Matter of Tiffany Street and East River*); *In re Coney Island Hotel Corp.*, 76 F. (2d) 126 (C. C. A. 2nd)—order of dismissal signed March 26, 1935—order appointing trustee signed December 11, 1935 (Supreme Court, Kings County, #14,668/1933, *sub. nom. Matter of Bond & Mortgage Guarantee Co. (Half Moon Hotel)*; *In re Manbeach Realty Corp.*, 10 F. Supp. 523 (D. C., E. D. N. Y.)—order of dismissal signed April 28, 1936—order appointing trustee and approving extension and modification plan signed March 18, 1936 (Supreme Court, Kings County, #14,668/1933, *sub nom. Matter of Bond & Mortgage Guarantee Co. (2981 Sea Air Avenue)*. The mortgage reorganized and later remitted to the state court was: *Matter of Ashwood Realty Corp.* (S. D. N. Y. #60,455)—order approving plan of reorganization signed August 8, 1935, *In re Ashwood Realty Corp.*, decided February 24, 1939, no opinion (see 37 F. Supp. 670), permitting State Mortgage Commission to modify plan in state court, order relinquishing jurisdiction signed March 21, 1939—order appointing permanent trustee signed by Frankenthaler, *J.*, September 20, 1939 (Supreme Court, New York County, #14,245/1939), *sub nom. Matter of 400 East 58th Street, Manhattan.* The three mortgages reorganized in the federal court were: *In re Island Park Associates*, 77 F. (2d) 334 (C. C. A. 2nd)—order signed confirming plan pursuant to which Title Guarantee and Trust Company purchased all outstanding certificates against the large properties involved and a composition between Title Guarantee and Trust Company and the debtor was approved, *Matter of Island Park Associates, Inc.* (E. D. N. Y. #27,300); *Matter of 455 West 34th Street Corp.* (S. D. N. Y. #61,923); *Matter*

SECOND. The dismissal of the petition was correct because it is unreasonable to expect that a plan of reorganization can be effected.

We realize that mere insolvency in the bankruptcy sense need not necessarily result in a dismissal of a petition at its inception. In some cases it is reasonable to expect that the debtor will raise new money to preserve a good will in the business. *In re Dutch Woodcraft Shops,* 14 F.

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of Wadsworth Gardens, Inc. (S. D. N. Y. #62,161)—in both the latter cases the order decreed the debtor insolvent and directed sale of the property and appointment of a permanent trustee of the purchase money mortgage.

Seven cases, in addition to the instant case, have arisen after the appointment of a Schackno trustee. In all but one of such cases the petition has been dismissed; in one such case the federal court retained jurisdiction. Those cases dismissed were: *In re Paloma Estates,* 126 F. (2d) 72; *In re Blinrig Realty Corporation,* 114 F. (2d) 100; *Brooklyn Trust Co.* v. *Rembaugh,* 110 F. (2d) 838; *In re Reliable Estates,* 33 F. Supp. 588 (D. C., E. D. N. Y.); *Matter of Chelsea Presbyterian Church* (S. D. N. Y. #73,084); *In re Amawalk Nursery, Inc.* (S. D. N. Y. #60,774). The one case in which the petition was approved was *In re Castle Beach Apartments,* 113 F. (2d) 762, which has already been discussed, *supra* p. 29. In that case, the debtor had purchased the mortgaged property for a very large sum in 1935. The petition asserted an equity of over $50,000 above the mortgage. (Record on appeal, p. 7). The debtor in its brief in the Circuit Court of Appeals argued that insolvency had not been shown, and the Chapter X trustee in his brief stated (p. 8):

> "On the question whether the debtor has any equity, this appellee takes no position, except to point out that this question has not as yet been fully investigated in this proceeding."

Ultimately, the debtor was eliminated from the proceeding because it was found to have no equity and the "reorganization" consisted of the formation by certificate holders of a corporation to take title to the premises (S. D. N. Y. #75,836).

Supp. 467, 471 (D. C., W. D. Mich.); *Case* v. *Los Angeles Lumber Products Co.*, 308 U. S. 106; *Kansas City Ry.* v. *Cent. Union Tr. Co.*, 271 U. S. 445, 455. It is sometimes even reasonable to permit a Chapter X proceeding to continue so that there may be a slow and orderly liquidation. *R. L. Witters Associates* v. *Ebsary Gypsum Co.*, 93 F. (2d) 746 (C. C. A. 5th); *In re Central Funding Corp.*, 75 F. (2d) 256 (C. C. A. 2nd).

But where there is no good will, but simply an apartment house with mortgage indebtedness upon it largely exceeding the value of the premises, there is certainly no reason to require the only interested parties, the certificate holders, to bear the expense of a useless and hopeless Chapter X proceeding. In *Tennessee Publishing Co.* v. *American National Bank*, 299 U. S. 18, 22, this court said:

> "Nor do we need to inquire as to the precise limits of the concept of 'good faith' as required by § 77B. Whatever these limits may be, the statute clearly contemplates the submission of a plan of reorganization which admits of being confirmed as *'fair and equitable'* and as *'feasible.'* However honest in its efforts the debtor may be, and however sincere its motives, the District Court is not bound to clog its docket with visionary or impracticable schemes for resuscitation. Sub-section (f) of § 77B provides for the confirmation of a plan only if the District Judge is satisfied '(1) that it is fair and equitable and does not discriminate unfairly in favor of any class of creditors or stockholders, and is feasible.' These are prime conditions. Unless the District Judge finds that the plan has these qualities he need go no further. Unless he so finds, he has no authority to proceed."

Unless the debtor puts in new money, only a plan of reorganization which gives the entire property to the certificate holders would be considered a fair one. *Reading Hotel Corp.* v. *Protective Committee,* 89 F. (2d) 53 (C. C. A. 3d) cert. den., 302 U. S. 742. Plans of reorganization which permit a debtor, holding a parcel of real estate, its stockholders or junior creditors, to participate under the circumstances existing in this case, have regularly been declared unfair by the courts under Section 77B. *Metropolitan Holding Company* v. *Weadock,* 113 F. (2d) 207 (C. C. A. 6th); *Whitmore Plaza Corp.* v. *Smith,* 113 F. (2d) 210 (C. C. A. 6th); *Sophian* v. *Congress Realty Co.,* 98 F. (2d) 499 (C. C. A. 8th); *Highland Towers Co.* v. *Bondholders' P. Committee,* 115 F. (2d) 58 (C. C. A. 6th).

Here it is obvious that the debtor cannot, will not and does not intend to put up any new money. In paragraph 13 of the petition the debtor swore:

> "13. The purpose of this proceeding is to procure a readjustment of the corporate structure, and all its secured indebtedness, so as to extend the time of payment of said secured indebtedness, upon such terms as will enable the debtor to pay a reasonable amount annually in reduction of the principal thereof in accordance with the provisions of a plan of re-organization to be presented to this Court" (R. 84).

True there are unsupported statements in the papers filed in support of the petition to the effect that new moneys may be made available "if a satisfactory re-organization is consummated" (R. 84, 64), but no indication is given as to who will supply such moneys and it is hard to believe under the circumstances of this case that anyone will do so unless

certificate holders reduce the amount of their mortgage to a point which creates some equity for the debtor (R. 68). Such a plan was disapproved as unfair in *In re Day & Meyer, Murray & Young*, 93 F. (2d) 657 (C. C. A. 2nd), even though the reduction in the first mortgagee's interest was approved by a majority of the first mortgage bondholders.

The courts have in many instances dismissed proceedings under Section 77B and Chapter X either at the outset or during the course of the proceedings, as soon as it became obvious that it was not reasonable to expect that a fair plan could be effected and that no good purpose would be served by permitting the proceedings to continue. *Chapman Bros. Co.* v. *Security-First National Bank*, 111 F. (2d) 86 (C. C. A. 9th), cert. den., 311 U. S. 652, petition under Chapter X dismissed *at the outset* at request of mortgagee where debtor had no equity; *Seaboard Terminals Corp.* v. *Western Maryland Ry. Co.*, 108 F. (2d) 911 (C. C. A. 4th), petition under Chapter X dismissed *before any plan filed* upon showing that debtor had no property to reorganize; *In re Suburban Properties*, 110 F. (2d) 438 (C. C. A. 7th), petition under Chapter X dismissed *at outset* where debtor had no equity and state foreclosure was pending; *In re Corn Kelly Corp.*, 32 F. Supp. 572 (D. C., E. D. N. Y.), aff'd 111 F. (2d) 644, petition under Chapter X dismissed *at outset* where debtor had no equity in real estate being foreclosed in state court; *In re Ware Metal Products*, 42 F. Supp. 538 (D. C., D. Mass.), petition under Chapter X dismissed *at outset* as not in good faith where reorganization was not feasible; *San Francisco Laundry Ass'n* v. *American Trust Company*, 127 F. (2d) 187 (C. C. A. 9th)—petition under Chapter X dismissed *after plan*

filed, where debtor was insolvent and plan was not feasible; *Manati Sugar Co.* v. *Mock,* 75 F. (2d) 284 (C. C. A. 2nd), petition under Section 77B dismissed *at outset* as not feasible and not in good faith; *Price* v. *Spokane Silver & Lead Co.,* 97 F. (2d) 237 (C. C. A. 8th), cert. den., 305 U. S. 626, petition under Section 77B dismissed *after plan filed* where debtor had no equity and prior state court receivership was pending; *Wayne United Gas Co.* v. *Owens-Illinois Glass Co.,* 91 F. (2d) 827 (C. C. A. 4th); petition under Section 77B dismissed *after plan submitted* where debtor had no equity and prior state court mortgage proceeding was pending; *O'Connor* v. *Mills,* 90 F. (2d) 665 (C. C. A. 8th), petition under Section 77B dismissed *after plan filed* where debtor had no equity and federal receivership and foreclosure suit was pending; *Provident Mut. Life Ins. Co.* v. *University Ev. L. Church,* 90 F. (2d) 992 (C. C. A. 9th), petition under Section 77B dismissed *after plan filed,* where plan was visionary and foreclosure proceedings had progressed to sale of the property; *Reighard* v. *Higgins Enterprises,* 90 F. (2d) 569 (C. C. A. 3d), petition under Section 77B dismissed *after plan filed* where plan was not feasible, the debtor had no equity and state foreclosure proceedings were pending; *In re Williamsport Wire Rope Co.,* 10 F. Supp. 481 (D. C., M. D. Pa.), aff'd 78 F. (2d) 1023, petition under 77B dismissed *after plan filed* where plan was impracticable and equity receivership was pending. See also *In re 620 Church Street Bldg. Corp.,* 299 U. S. 24, where this court held that the debtor, its stockholders and junior lienors had no right to appeal after confirmation of a plan of reorganization in 77B proceedings, because they had no equity in the property; *In re Schulte-United,* 50 F. (2d) 243 (D. C., S. D. N. Y.), where a bankruptcy court

allowed mortgagee to foreclose in state court because bankrupt had no equity in the mortgaged property; *Lincoln-Alliance Bank & Trust Co.* v. *Dye*, 115 F. (2d) 234 (C. C. A. 2nd), where mortgagee was permitted to foreclose in state court despite pending Chapter X proceeding because debtor had delayed in formulating a plan; *First National Bank* v. *Conway Road Estates Co.*, 94 F. (2d) 736, 739 (C. C. A. 8th), cert. den., 304 U. S. 578.

It is also unreasonable to expect that a plan of reorganization can be effected, because the mortgage trustee opposes any plan in the Federal court. It is unreasonable to expect that a plan of reorganization can be effected when the granting of a petition is opposed by a creditor such that, even if a plan were to be evolved, attempts to secure approval of the plan would necessarily fail; and the same rule applies when opposition to a petition comes from a preponderant majority of a single class of creditors. *Manati Sugar Co.* v. *Mock*, 75 F. (2d) 284, 285 (C. C. A. 2nd); *In re North Kenmore Building Corp.*, 81 F. (2d) 656 (C. C. A. 7th) (82% of bondholders objected); *In re City Bond and Mortgage Corp.*, CCH Bankruptcy Law Service, ¶ 8118.01; Dec. ¶ 4512; *In re Hotel Park Central, Inc.*, CCH Bankruptcy Law Service, ¶ 8116.03; Dec. ¶ 3545 (92% of bondholders objected); *In re Coronado Hotel Co.*, CCH Bankruptcy Law Service, ¶ 8116.03; Dec. ¶ 3002; *Finletter, The Law of Bankruptcy Reorganization* (1939), p. 60; see Section 216, subd. 7 of Chapter X; 11 U. S. C. 616 (7).

As respects the debtor's petition in the instant case, the respondent Schackno trustee stands in the position of a single first mortgagee or of a unanimous class of first

mortgage bondholders. It, rather than the certificate holders, is the creditor whose assent to any plan is necessary within the meaning of Chapter X. Section 106 subdivision (4) (11 U. S. C. 506(4)) defines a "creditor" as "the holder of any claim". See also Section 197 (11 U. S. C. 597). All claims which certificate holders (as distinguished from Title Guarantee and Trust Company which held legal title to the mortgage, and from Bond and Mortgage Guarantee Company which held reserve powers to enforce the mortgage) formerly held against the debtor were transferred to the Schackno trustee when the Shackno trust was created. *In the Matter of Dalton Schools, Inc.*, D. C., S. D. N. Y. #80,480, *Weil* v. *President and Directors of Manhattan Company*, 275 N. Y. 238; *Matter of People (Tit. & Mtge. Guar. Co.)*, 264 N. Y. 69. See *E. T. C. Corp.* v. *Title Guar. & Trust Co.*, 271 N. Y. 124; *Jacoby* v. *Bond & Mortgage Guarantee Co.*, 72 F. (2d) 420 (C. C. A. 2nd).

Not only does the Schackno trustee have legal title to the bond and mortgage; it also has full and exclusive power to enforce the claims represented by each of those instruments. It was appointed trustee by a valid final order of a court of record of the State of New York through consent of over 66⅔% of certificate holders (R. 42). Pursuant to that order the bond and mortgage were assigned by Title Guarantee and Trust Co. to respondents' predecessor, and the Mortgage Commission, as the holder of any residuum of rights once held by Bond and Mortgage Guarantee Company, joined in the assignment (R. 12). In the same final order, the court directed the execution of a specific declaration of trust (R. 43) which declaration of trust establishes the powers and duties of the trustee

(*Matter of People* [*Lawyers West. Mtg. & Title Co.*], 288 N. Y. 40). By the terms of that declaration of trust the trustee is "vested with all the rights and powers of an absolute owner of the property * * * constituting the Trust Estate and may exercise any and all such rights and powers" (R. 24). The trust estate includes "the bond and mortgage * * * against which were issued the Mortgage Certificates * * * together with all claims and choses in action which Certificate Holders as a class have or may have against any person, firm or corporation with respect to any of the property now or formerly included in the Trust Estate" (R. 23-24). The trustee is specifically empowered "to enforce the claims of the certificate holders as a class against the above named guarantee company and against *any other* person, firm or *corporation*" (R. 25).

In *Matter of People* (*Tit. & Mtge. Guar. Co.*), 264 N. Y. 69, the Supreme Court had approved a reorganization plan directing the depositary of a pool of mortgages* to deliver all the deposited collateral to "Buffalo Series R Corporation", whose certificate of incorporation provided:

> "The corporation shall have all of the right, title, interest and powers of an individual owning said bonds and mortgages and other property and securities in his own name" (Record on Appeal from order of January 8, 1934, fol. 66).

In affirming this order, the court said (pp. 86-87, 92):

> "Ordinarily the holder of certificates of an interest in guaranteed mortgages has no rights or

*Though that case involved a pool of mortgages, the same principles apply to a single mortgage covering a specific piece of property like the one at bar. *Matter of People* (*Westchester Tit. & T. Co.*), 268 N. Y. 432, 439-440.

duties in connection with the mortgage at least as long as the guaranty company is doing business and complies with its own undertakings. The guaranty company under its contract with the holder of the certificate may decide whether to foreclose or extend the mortgage, to waive or to resort to a remedy for any default. * * * when the guaranty company ceases to conduct business, some other person or corporation, must be substituted for it, authorized to administer or, at least, to enforce the mortgage investments in which all the certificate holders are interested.

* * * * * * *

"The essential purpose of the statute is * * * to provide for the adoption of a plan for the permanent administration of the mortgage investments in which groups of investors are interested."

If all rights of ownership in the mortgage herein had been similarly transferred to a corporation, this proceeding could not be entertained over its opposition, on the theory that the stockholders were the real creditors. No different rule should apply in the thousands of reorganizations where these rights of ownership were transferred to trustees instead, pursuant to express statutory authority. In *Montgomery* v. *M'Dermott*, 103 Fed. 801 (C. C. A. 2nd), one McHenry conveyed certain property to trustees as security for a debt. Certificates of participation were issued to McHenry and to the creditor. The court said (pp. 805-806):

"It was an absolute conveyance, and carried the full legal title, with no reservation whatsoever. Thereafter the grantor had no specific individual interest in any specific piece of property so conveyed * * *. His interest in the corpus of the trust was still

> property, but it was not tangible property. It was an equitable interest, which he could enforce only through the aid of a court of equity, constraining the trustees to carry out the trust, and thus get funds in their hands, and, having carried it out, to account for his proportion of the net proceeds of their operations."

The Schackno trustee is not an "indenture trustee" within the meaning of Chapter X and the judge in the Chapter X proceeding is not entitled by Section 212 (11 U. S. C. 612) to "examine and disregard" any provision of the declaration of trust or to "restrain the exercise of any power" under such declaration. An indenture trustee for the purposes of Chapter X is defined by Section 106, subdivision 8 (11 U. S. C. 506 (8)) as "a trustee under a mortgage, deed of trust, or indenture, pursuant to which there are securities outstanding. * * * constituting claims against a debtor or claims secured by a lien upon any of its property". Respondent is not "trustee under a mortgage, deed of trust, or indenture" because the declaration of trust under which it is acting pursuant to the enabling provisions of the New York statutes is not a mortgage, deed of trust or indenture. The declaration of trust has none of the essential attributes of a mortgage or deed of trust. Indentures are defined by the dictionaries as formal written instruments made between two or more persons in different interests. See 2 Bouvier's Law Dictionary; Schumaker and Longsdorf's Cyclopedic Law Dictionary; *Scott* v. *Mills*, 10 New York State Reporter 357, 358. Here the declaration of trust is executed by the Schackno trustee alone, pursuant to court order entered under the provisions of the statute. (R. 36).

Nor is respondent a trustee under an instrument "pursuant to which there are securities outstanding". The certificates, which are the "securities outstanding" in this case, were issued many years ago by Title Guarantee and Trust Company and guaranteed by Bond and Mortgage Guarantee Company. The certificate holders have consented to a "plan of reorganization" under the Schackno Act promulgated by the Mortgage Commission and approved by the court which has resulted in the execution of the declaration of trust under which the trustee is acting. The declaration of trust has been formulated pursuant to the consent of the certificate holders; the certificates are not outstanding *pursuant to* the declaration of trust. Whatever ambiguity might exist in the meaning of the word "outstanding" as used in the statutory definition of an indenture trustee is removed by the "Sectional Analysis of Chapter X" in Senate Report No. 1916 (75th Cong. 3d. Sess; May 27, 1938) at page 23. With reference to Section 106 (8), the Report reads as follows:

> " 'Indenture trustee' (8) is a significant addition to the definition section of the chapter, reflecting as it does the enlarged role which such trustees may play thereunder in representing and safeguarding the interests of securities *issued* pursuant to such indentures."

Section 198 of the Act lends added emphasis to the fact that the term "indenture trustee" meant to the drafters of the Act a trustee designated in a trust instrument pursuant to which securities had been *issued*. Section 198, in so far as it is pertinent, reads:

> "An indenture trustee may file claims for all holders, known or unknown, of securities *issued*

pursuant to the instrument under which he is trustee, who have not filed claims."

If the Schackno trustee were an indenture trustee it would be barred by Section 198 from filing claims on behalf of certificate holders since the certificates are not "securities issued pursuant to the instrument under which [it] is trustee". This cannot be the intention of Chapter X.

Accordingly we submit that the respondent, the Schackno trustee, must be treated as the first mortgage creditor and not as an indenture trustee, and since there is no equity above the first mortgage, no reorganization can be effected without respondent's consent. *Louisville Bank* v. *Radford*, 295 U. S. 555, 585-6, 594-5; *In re Murel Holding Corp.*, 75 F. (2d) 941, 942 (C. C. A. 2nd); *In re Prudence Co.* (*Reconstruction Finance Corporation* v. *Prudence Co., Inc.*), 90 F. (2d) 587, 589 (C. C. A. 2nd). It is as though the Schackno trustee were trustee under a will or *inter vivos* trust, in which event there would seem to be no question but that the trustee rather than the beneficiaries of the trust would vote in a Chapter X proceeding.

Although the Circuit Court for the Second Circuit, in *In re Blinrig Realty Corporation*, 114 F. (2d) 100 and in *In re Castle Beach Apartments*, 113 F. (2d) 762, rejected a similar argument by Schackno trustees in opinions which merely stated the Court's conclusion on the point, two opinions in the Southern District of New York have discussed the point at length and have sustained the Schackno trustee's contention. In *Matter of Amawalk Nursery, Inc.*, S. D. N. Y., #60,774, the District Court held that a Schackno trustee's opposition to 77B proceedings was sufficient reason for dismissal of those proceedings. In *Matter*

of Dalton Schools, Inc., S. D. N. Y., #80,480, decided October 1, 1942, the Special Master filed a report ruling that after the appointment of a Schackno trustee, the trustee alone, to the exclusion of the certificate holders, was entitled to file claims against the debtor in a Chapter X proceeding.

We believe it is particularly important that the paramount right of certificate holders should be considered in this case. The debtor defaulted on its interest and taxes although the earnings of the property were sufficient to cover such items (R. 12, 16) and thus cut off the income of certificate holders who are dependent upon such income. The debtor then permitted foreclosure proceedings to continue for four and a half months before filing a petition under Chapter X. It seems to us obvious that it is the hope of the debtor (which contends that certificate holders must act for themselves rather than through respondent) that it will be able to use the need of the certificate holders to its advantage and to persuade them, in view of the delay and expense which would confront them in a Chapter X proceeding, to accept some plan of reorganization which would give the debtor an equity in the mortgaged property that does not now exist or some chance to gain an income from the property at the expense of certificate holders. Under such circumstances we believe the federal courts are not only justified in dismissing but are required to dismiss the proceedings at the outset rather than to permit them to continue with resultant expense and no possibility of benefit to certificate holders.

Conclusion

The order of the Circuit Court of Appeals should be affirmed.

Respectfully submitted,

CHARLES E. HUGHES, JR.,
CURTISS E. FRANK,
Counsel for Respondent
Manufacturers Trust Company.

FILE COPY

FILED
OCT 19 1942
CHARLES ELMORE CROPLEY
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1942.

No. 24

MARINE HARBOR PROPERTIES, INC.,
Petitioner,

against

MANUFACTURERS TRUST COMPANY (successor by merger to The Mortgage Corporation of New York), as trustee for the benefit of certificate holders in mortgage guaranteed by Bond and Mortgage Guarantee Company, Guarantee #181,568,
Respondent,

MAURICE RUBINGER, trustee of Marine Harbor Properties, Inc.,

SAMUEL SILVERMAN, additional trustee of Marine Harbor Properties, Inc.,

MORTIMER RUBENSTEIN, foreclosure-receiver,

and

SECURITIES AND EXCHANGE COMMISSION

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

MOTION OF CERTAIN CHARITABLE INSTITUTIONS FOR LEAVE TO FILE BRIEF AS *AMICI CURIAE*, AND BRIEF OF *AMICI CURIAE*

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Counsel for The Domestic and Foreign Missionary Society of the Protestant Episcopal Church in the United States of America

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MOTION FOR LEAVE TO FILE BRIEF AS *AMICI CURIAE*

May it Please the Court:

The undersigned, as counsel for the charitable institutions listed below, respectfully move this Honorable Court for leave to file the accompanying brief in this case as *amici curiae.*

MARTIN A. SCHENCK,
Counsel for The Domestic and Foreign Missionary Society of the Protestant Episcopal Church in the United States of America

SAMUEL KRAMER,
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AS *AMICI CURIAE.*

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and

SECURITIES AND EXCHANGE COMMISSION

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF OF CERTAIN CHARITABLE INSTITUTIONS, *AMICI CURIAE*

PRELIMINARY STATEMENT

This brief is submitted on behalf of *The Domestic and Foreign Missionary Society of the Protestant Episcopal Church in the United States of America, Society for Experimental Biology and Medicine—College of the City of New York, The Mount Sinai Hospital, Board of National Missions of the Presbyterian Church in the United States of America, Brooklyn Thoracic Hospital, Brooklyn Public Library, Brooklyn Hebrew Home and Hospital for the Aged, House of St. Giles the Cripple, Trustees of St. Patricks Cathedral in the City of New York and Catholic Missionary Union*, as *amici curiae*, in opposition to the contention of petitioner and of the Securities and Exchange Commission that the certificated mortgage involved in the above entitled action, which is typical of thousands of certificated mortgages reorganized in permanent liquidating trusts in the New York State courts, should be made the subject of further reorganization in the federal court through the instrumentality of a debtor's petition under Chapter X of the Bankruptcy Act.

This brief is filed with the written consent of the petitioner and the respondent. The Securities and Exchange Commission, which intervened in the proceedings upon its own motion pursuant to Section 208 of Chapter X, has refused to grant consent.

These *amici curiae* are charitable institutions operated on a non-profit basis for the benefit of the public welfare. These institutions have invested in and presently hold a substantial amount of guaranteed first mortgage certificates similar to the type involved in this action. These mortgages (hereinafter sometimes referred to as "Schackno mortgages") have been reorganized in the

New York State Supreme Court under the Schackno Act (New York Laws of 1933, c. 745) or the Mortgage Commission Act (New York Laws of 1935, c. 19) and are now being liquidated by permanent trustees appointed in such reorganizations. This case has been characterized by the Securities and Exchange Commission as a test case (*Memorandum of Securities and Exchange Commission in support of application for certiorari*, pp. 12-13) to "determine whether the federal procedure provided by Chapter X shall be available for * * * further reorganization" of Schackno mortgages. Since these charitable institutions are certificate holders in many of these Schackno mortgages, their interests may well be directly affected by the decision in this case.

ARGUMENT

The facts in this action are set forth in detail in the briefs of the respondent Manufacturers Trust Company and of The People of the State of New York. We are in complete accord with the arguments in those briefs and believe that the Schackno trust proceedings pending in the state court will best subserve the interests of certificate holders and that further reorganization in the federal court would only result in additional unnecessary delay and expense.

In filing this brief, we wish to emphasize the importance of this litigation to Schackno mortgage certificate holders. More than $700,000,000 in principal amount of certificated mortgages have been reorganized in the New York Supreme Court during the past nine years (*Respondent's Brief*, pp. 17-18). Most of these mortgages are now being liquidated in the state courts by qualified trustees of considerable experience under the continuing

supervision of judges especially assigned to this work, who are aided by experts as exemplified, in the Second Judicial Department, by the Bureau of Trust Supervision. These judges and their advisory personnel have had a long experience with the reorganization of these mortgages and are fully familiar with all phases of the problem. The complete history of each mortgaged property is available to them for reference in determining the fairness and feasibility of any plan of reorganization. The declaration of trust under which Schackno trustees operate was developed through the combined efforts of New York State officials and attorneys specializing in this field. All these factors have resulted in the success of the New York State procedure for the reorganization and continuing liquidation of these mortgages.

At the present time most of the issues are paying interest regularly and also amortizing the principal (see *Report of Bureau of Trust Supervision*, p. 19). The income from these securities is of vital importance to these charitable institutions. A new reorganization in the federal courts would merely mean an expense to the trust estate with a consequent reduction in income to certificate holders for which there would be no compensating benefits. Any procedure which involves delay and consequent stoppage of income would be a serious disadvantage to these institutions, which are partially dependent upon income from investments for the continuance of their charitable activities. The instant case well illustrates the interference with continuity of income which results from a wilful default by a mortgagor (debtor) and subsequent litigation arising from its efforts to initiate a Chapter X proceeding. If foreclosure were permitted to take its normal course, the period of interference with the certifi-

cate holders' income would undoubtedly be held to a minimum.

We respectfully submit that the permanent liquidating trusts set up by the New York Supreme Court are presently operating in a fair, economical and completely satisfactory manner and that to disregard ten years of effort on the part of the New York State officials and courts and permit the initiating of new proceedings in the federal court would be unwise, unnecessary, expensive, inefficient and detrimental to the best interests of certificate holders.

CONCLUSION

The order of the Circuit Court of Appeals should be affirmed.

Respectfully submitted,

MARTIN A. SCHENCK,
Counsel for The Domestic and Foreign Missionary Society of the Protestant Episcopal Church in the United States of America

SAMUEL KRAMER,
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AS *AMICI CURIAE.*

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MORTIMER RUBENSTEIN, Foreclosure-Receiver, and

SECURITIES AND EXCHANGE COMMISSION.

BRIEF OF PEOPLE OF THE STATE OF NEW YORK, AMICUS CURIAE

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MORTIMER RUBENSTEIN, Foreclosure-Receiver,

and

SECURITIES AND EXCHANGE COMMISSION.

BRIEF OF PEOPLE OF THE STATE OF NEW YORK, AMICUS CURIAE

The People of the State of New York submit this brief as *amicus curiae* because they have a two-fold interest in the subject of this litigation. The Securities and Exchange Commission, in its brief, and the dissenting judge in the

Circuit Court maintain that the interests of creditors would not be best subserved in the pending State Court proceeding. The State of New York is submitting this memorandum to direct this Court's attention to the important steps taken by the State of New York for the protection of mortgage certificate holders. The analysis of the history and development of the State Court procedure over a period of ten years will show that the legislative and administrative safeguards provided in such proceedings for the protection of mortgage certificate holders (the only parties interested in the instant case) are more effective than those contained in Chapter X of the Bankruptcy Law with respect to the peculiar local problems here involved. This, coupled with the fact that the creditors in a Chapter X proceeding will necessarily be put to considerable and needless expense and delay in a Chapter X proceeding, which must, in the circumstances of the instant case, prove futile, will demonstrate that the interests of mortgage certificate holders would be best subserved in the pending State Court proceedings. The State of New York is further interested because the Superintendent of Insurance of the State of New York, acting as liquidator of various title and mortgage companies for the benefit of creditors of those companies, owns certificates in excess of $1,000,000 which will be affected by this litigation.

Opinions Below

The opinion of the District Court (Bright, D. J.) is contained in the record (R. 70-75) and is also reported in 41 F. Supp. 814. The majority (Swan, C. J., and Chase, C. J.) and dissenting (Frank, C. J.) opinions of the Circuit Court of Appeals are contained in the record (R. 107-126) and are also reported in 125 F. (2d) 296.

Jurisdiction

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925.

Statutes Involved

Section 141 of Chapter X of the Bankruptcy Act (11 U. S. C., Sec. 541) provides:

"§ 141. Petition of Debtor.

Upon the filing of a petition by a debtor, the judge shall enter an order approving the petition, if satisfied that it complies with the requirements of this chapter and has been filed in good faith or dismissing it if not so satisfied."

Section 146 (11 U. S. C., Sec. 546) provides in part as follows:

"§ 146. Good faith of Petition.

Without limiting the generality of the meaning of the term 'good faith', a petition shall be deemed not to be filed in good faith if—

* * * * * * *

(3) it is unreasonable to expect that a plan of reorganization can be effected; or

(4) a prior proceeding is pending in any court and it appears that the interests of creditors and stockholders would be best subserved in such prior proceeding."

Statement of the Case

The relevant facts are set forth in the brief of the Manufacturers Trust Company, as Trustee, and in the majority opinion (R. 106-111) and will not be here repeated.

Question Presented

The question herein is whether, under the above statute (Sec. 141 of Chap. X of the Bankruptcy Act) a corporate mortgagor, with no assets other than an improved parcel of real property which is encumbered by a certificated first mortgage larger in amount than the value of the said property, may force the holder of said mortgage into a Chapter X proceeding where proceedings have already been had under State statutes specifically designed to safeguard the rights of first mortgage certificate holders and in which proceedings the debtor has participated.

Argument

We shall not discuss herein the various arguments made in the brief of the respondent Manufacturers Trust Company, as Trustee. We believe the points it makes are well taken and we rest upon them. We shall, however, place our emphasis upon the adequacy of the State Court proceedings to protect creditors of the type here involved. In our opinion, the conclusions stated in the following excerpt from the prevailing opinion (R. 110) are correct and should be sustained in this Court:

> "But the debtor made no attempt to bring its proposals to the attention of the state court in the pending proceeding, as we think it was entitled to do as an 'interested party'; had it done so its proposals, with the court's approval, could have been presented to the certificate holders. That proceeding provides adequate means to reorganize the mortgage and protect the rights of all certificate holders whose interests alone exhaust the debtor's property."

We contend that the interests of certificate holders will best be subserved in the pending State Court proceedings and that there is no necessity for any further reorganization.

We shall show to this Court that the State of New York, as a matter of legislative policy, has been deeply concerned for more than nine years with the protection and reorganization of the rights of guaranteed mortgage certificate holders and that this duty of the State to certificate holders has been and is being discharged in an able and efficient manner by the Bureau of Trust Supervision and the liquidating trusts appointed by the State Supreme Courts. The transfer of these proceedings to the Federal Court is unnecessary and will result in additional expense and delay to the certificate holders. Because of the peculiar complexity of this local problem, it is in the certificate holder's interest that it be permitted to solved in the pending State Court proceedings.

The Securities and Exchange Commission, in its brief, states that the emergency statutes enacted by the State of New York recited as their purpose the protection of the guaranty companies against claims on guarantees. This is not the case. These statutes had as their main objective the protection of the rights of certificate holders. A reading of the statutes would so demonstrate very clearly (see *McKinney's Unconsolidated Laws*, Secs. 4801, 4871). The debtor-petitioner is guilty of the same misconception in its brief. Nor do we understand the debtor's claim that certificate holders were brought into the State Court against their will. More than 66⅔% of the certificate holders actually consented (R. p. 10).

The statement is made in the dissenting opinion which indicates that the dissenting Judge believed the certificate holders in the State Court proceedings not to be at all informed or protected as to their rights. This argument will be met later in this brief (p. 15).

The Securities and Exchange Commission in its brief claims that under the New York laws there are lacking almost all of the basic safeguards for the protection of security holders as found in Chapter X. It will be shown that this claim is entirely without basis, as is also the criticism of the State Court proceedings by the dissenting Judge.

The Securities and Exchange Commission did not appear in this proceeding until after the District Court had rendered its decision. The Commission and the debtor make the argument, in common with Judge Frank of the Circuit Court of Appeals, that the adequacy and desirability of the pending proceedings in the State Court must be proved by the trustee, but that the advantages of the proceedings under Chapter X follow as a matter of course and need no proof.*

In our opinion, the burden of proof was on the petitioner to show that the pending State proceedings would not best subserve the interests of creditors. However, the issue of the efficacy of the State proceedings having been raised, we believe that the present state of the record makes it advisable for the State of New York to submit, for the information of the Court, the history of the steps taken by the Legislature, by the Courts and by the administrative officers of the State of New York, all in the interests of the creditors. The facts stated are taken from public records compiled during the course of administration by the various departments of the State government and on file, available for public examination.

FIRST: The interests of creditors will be best subserved in the State Court proceedings.

Outline of the Mortgage Guarantee Business

The guaranteed mortgage business was confined almost exclusively to the City of New York and its neighboring communities. The properties which underlie the guarantees were similarly located. The problem is not nation-wide—it is a local problem confined mainly to the metro-

* It should be pointed out that because of the failure of the Securities and Exchange Commission to intervene in the District Court the record is not ideally suited to the determination of the underlying question in this appeal.

politan area in the State of New York (see Note, 34 Columbia L. Rev. 664). The general method of doing business was for the guaranty company to make mortgage loans with its funds and then to sell the mortgages or certificates therein to investors with its guarantee. The companies reserved to themselves the right to administer the mortgages. The securities issued by these companies fell generally into two classes: (a) guaranteed whole mortgages, where a single mortgage, with guarantee, was sold in its entirety to an investor; and (b) guaranteed participation certificates, where fractional shares were sold in a single mortgage or in a group of mortgages.

The instant case concerns itself with the certificated type of guaranteed mortgage and not with the guaranteed whole mortgage.

Activity of the Legislature and of the Superintendent of Insurance

Acting under Article XI (now Art. XVI) of the Insurance Law of this State and Chapter 40 of the Laws of 1933, the Superintendent of Insurance took over the guaranty companies for rehabilitation in August of 1933, when, because of general economic distress in the real estate field, these companies were unable to meet the obligations of the guarantees. On December 31, 1933, there were outstanding approximately 20,000 guaranteed mortgages against which certificates had been issued and which were held by more than 200,000 persons. The aggregate of principal amount was $815,610,435.35 (*The Administration of Delinquent Title and Mortgage Guaranty Companies*, by George S. Van Schaick, May 10, 1935, p. 18, exhibit; Report to the Governor dated August 5, 1934, by George W. Alger, Commissioner, Appendices IV and V). In anticipation of the takeover of the certificated mortgages by the State, the Legislature enacted the Schackno Act (L. 1933, Ch. 745; *McKinney's Unconsolidated Laws*, Secs. 4871-4881), which became effective May 3, 1933, more than a year prior to Section 77-B of the Bankruptcy Act and more than five years prior to Chapter X of the Bankruptcy Act.

The State felt that it had a duty to protect the more than 200,000 certificate holders. The Legislature, in the concluding paragraph of the declaration of fact and policy in the Schackno Act, declared:

> "It is therefore hereby declared to be essential for the public interest to provide a procedure under which such bonds, mortgages or other security may be liquidated in an orderly manner and under which the assets of the guaranty corporations may be administered and conserved equally and ratably in the interests of holders of mortgage investments."

The Schackno Act (L. 1933, Ch. 745, Sec. 1) created a new remedy which was necessary to protect the rights of a vast number of certificate holders to prevent the demoralization of the real estate market, the wiping out of the equities of certificate holders and of owners and the general disruption of the financial structure (*Wolff* v. *Mortgage Commission*, 270 N. Y. 428, 432). This Act vested in the Superintendent of Insurance certain of the powers theretofore exercised by the guaranty companies, which powers included "provisions for safeguarding the interests of groups of holders of mortgage investments until a plan can be devised for permanent administration of these investments" (*Matter of People*, 264 N. Y. 69, 91). This statute made it possible to make effective such a plan for permanent administration by providing that after a hearing upon a proposed plan or agreement, upon twenty days' notice, the Supreme Court could approve such plan, which would become effective upon the consent of holders of two-thirds of the principal amount of the mortgage investment. The statute also recognized that the Court passing upon the plan should obtain the benefit of the judgment and experience of the administrative officer who had taken over the administration of these investments by providing that "the Superintendent should indicate to the Court whether or not he approves or disapproves such plan or agreement" (*McKinney's New York Unconsolidated Laws*, Sec. 4876(2)).

The Superintendent of Insurance created a Title and Mortgage Rehabilitation Bureau to supervise the administration of the title and mortgage companies in rehabilitation, including the certificated mortgages guaranteed by the companies (*The Administration of Delinquent Title and Mortgage Guaranty Companies*, supra, p. 20).

From September, 1933, to May 1, 1935, when the administration and control of the certificated mortgage issues were turned over to the Mortgage Commission (later described), mortgages in the principal amount of $324,850,161.59 had been partially or wholly reorganized by the Superintendent of Insurance (*The Administration of Delinquent Title and Mortgage Guaranty Companies*, supra, p. 43).

On April 27, 1934, a joint legislative committee was appointed to study the guaranteed mortgage situation. This committee recommended legislation to further the State's policy of relieving the unfortunate economic plight of the certificate holders and providing for the permanent administration of those investments.

Leg. Doc. 1934, Nos. 120, 121.

In 1934, the Legislature enacted a series of statutes to permit certificate holders to obtain loans on their certificates up to 25% of the face amount thereof (L. 1934, Chs. 912, 913, 914). The Governor of the State of New York, in his message to the Legislature on April 6, 1934 (Leg. Doc. 1934, No. 80), said:

> "These certificates are held by hundreds of thousands of people. Many of these people are of modest means. Some are destitute. Most have little experience with investments. All these conditions render the certificate holders particularly in need of protection and guidance."

An agency was obviously needed to give the certificate holders the benefit of expert legal and financial advice in reorganizing their mortgage certificate investments.

Activity of the Mortgage Commission

Thereafter, the Legislature created a new State agency known as The Mortgage Commission of the State of New York (*McKinney's New York Unconsolidated Laws,* Secs. 4801-4851), which commenced its activities in May, 1935. It was created for the purpose of administering the certificated issues, as successor to the Superintendent of Insurance. It was believed that it would be to the best interests of the certificate holders to have an agency administering the collateral which would not be encumbered with other duties. In order to facilitate the effectuation of reorganization plans which continued to require Court approval and the assent of two-thirds in amount of certificate holders, this statute provided "that assent to the plan need not be expressed affirmatively but that dissent from the proposed plan must be filed in writing and that those who fail to do so 'shall be conclusively deemed to have assented'" (*Matter of Mortgage Commission—1175 Evergreen Avenue,* 270 N. Y. 436, 442, aff'd *sub nom Lauro* v. *Barker,* 299 U. S. 521).

This statute likewise made available to the Court the judgment and experience of the administrative agency charged with the administration of these investments by providing for the submission by the Commission to certificate holders and the courts of plans involving extension and modification of mortgages coupled with the appointment of trustees to take over the permanent administration of the mortgages.

The Mortgage Commission reorganized during the period from May 1, 1935 to March 31, 1939, more than 13,500 mortgages whose aggregate principal was more than $583,000,000. Included in the latter figure is the amount of approximately $125,000,000 in mortgages which were in process of reorganization at the time of the turnover of these mortgages to the Mortgage Commission by the Superintendent of Insurance. Almost all of these reorganizations took place in the Supreme Court through the means

of the appointment or election of permanent trustees. The reorganizations were effected pursuant to the Schackno or Mortgage Commission Acts. In addition, there were principal reductions and cash liquidations on mortgages having a principal amount of $41,032,890.06 (*Annual Report of the Mortgage Commission,* April 1, 1939; Leg. Doc. 1939, No. 94, p. 17; *The Administration of Delinquent Title and Mortgage Guaranty Companies,* supra, p. 43).

The trustees so appointed or elected were similar in character to the respondent herein and act under declarations of trust similar to that which appears in this record (pp. 22-37).

The Legislature terminated the existence of the Mortgage Commission as of September 30, 1939, because it had promulgated reorganization plans with respect to more than 95% of the properties subject to its jurisdiction and had concluded the tasks imposed upon it by statute with respect to these reorganized mortgages (New York Session Laws of 1939, Ch. 944, Sec. 1). At the termination of the activities of the Mortgage Commission, the combined efforts of the two State agencies had resulted in liquidations and reorganizations of mortgages in excess of $800,000,000 in face amount. This left a balance in the approximate principal amount of $12,000,000, which was turned back to the Superintendent of Insurance on September 30, 1939. Between that date and September 30, 1942, he disposed of all but $2,141,197.59 of these mortgages, for the most part through reorganization by appointment of permanent liquidating trustees, pursuant to State statutes (Monthly Report of the Superintendent of Insurance Showing Disposition of mortgages, dated October 2, 1942).

The State has directly contributed approximately $2,000,000 of its own funds for the relief of certificate holders. This does not include the time and energy given to this task by the Superintendent of Insurance and other government officials and judges specifically assigned.

Between 1935 and 1939 New York State appropriated $1,330,950 from the general funds to cover the expenses of the Mortgage Commission which could not be directly allocated to any particular mortgage (see L. 1935, Ch. 56; L. 1936, Ch. 360; L. 1937, Ch. 125; L. 1938, Ch. 20; L. 1939, Chs. 460, 928). Two revolving funds, totaling $1,100,000, were also set up, to be used by the Mortgage Commission in reorganizing non-income producing properties (L. 1935, Ch. 290; L. 1937, Ch. 328). Without this fund, millions of dollars would have been lost by many thousands of certificate holders (Leg. Doc. 1938, No. 60). As of March 31, 1942, $761,973.13 was still outstanding in loans against these properties, much of which will never be collected. No interest was charged by the State for these loans. From 1939 to August, 1942, the State appropriated $325,000 for the use of the Superintendent of Insurance to conclude the work of the Mortgage Commission.

Activity of the Supreme Court of the State of New York

The judicial branch of the State Government co-operated in carrying out the comprehensive program of the State. In order to provide for uniformity of administration in reorganizing these certificated mortgages and in creating liquidating trusts, specific judges were designated by the Appellate Divisions to hold additional Special Terms of the Supreme Court in the respective judicial departments.

The Supreme Court, which was charged with the immediate responsibility for approval of these plans, decided that the rights of certificate holders would be better protected by vesting all the rights which an individual owning these bonds and mortgages would have, in trustees, rather than a corporation, because that would establish a fiduciary relationship and retain the right of supervision with the court (*Matter of New York Title & Mortgage Co.*, 153 Misc. 858, 864-866; *The Administration of Delinquent Title and Mortgage Guaranty Companies*, supra, p. 40; see also, *Matter of New York Title & Mortgage Co.*, 154

Misc. 447; *Matter of Lawyers Mortgage Co.*, 264 N. Y. 244). Express statutory authorization had been provided for the creation of such trusts (New York Session Laws of 1934, Ch. 920; New York Real Property Law, Sec. 96, subd. 5).

In the Second Judicial Department, out of which the present case arises, Mr. Justice George E. Brower was designated as the Justice to hear these matters, and has presided over all such proceedings from 1934 to date. Mr. Justice Brower, in almost all instances, except where a large majority of certificate holders, or one hundred percent of the certificate holders have requested appointment of individual trustees, has appointed corporate trustees of standing (Leg. Doc. 1939, No. 94, p. 7). These trustees have been appointed under a general plan of reorganization with a uniform Declaration of Trust, which was devised after much study and many conferences between the Court, the Mortgage Commission, the Insurance Department and attorneys familiar with this field of work. The form of such Declaration of Trust is set forth in the record (pp. 22-37). As appears in the Declaration of Trust, the purpose of the trust is to liquidate the mortgage investments as rapidly as possible; this liquidation to take place through amortizations on extensions, sales and satisfactions, all of which are, by the terms of the trust instrument, subject to the approval of the Court on notice to certificate holders. The trustee's fees are fixed by the Court within the annual maximum of ⅓ of 1% of the unpaid principal amount as fixed by the Trust Declaration and no attorneys' fees are permitted except in connection with court proceedings, and only if approved by the Court. The trustees are required to account annually. (See Report of Bureau of Trust Supervision, pp. 7, 8; *McKinney's Unconsolidated Laws*, Sec. 4815.)

The Declaration of Trust used in these cases has been described in the Report of the Securities and Exchange Commission, prepared by Mr. (now Justice) William O. Douglas, as follows:

"An unusually active type of trusteeship exists in New York State, in connection with the reorganization of issues of guaranteed mortgage certificates. Under the standardized form of declaration of trust * * * the trustee purports to be under a higher standard of obligation to the security holders than trustees under other indentures. Furthermore, he has expressed authorization to perform a broad range of acts looking toward future reorganizations. This type of trusteeship has developed out of a situation of unique complexity and peculiar difficulty. However, many features of the trusteeship itself seem to have no inherent restriction either to the type of security or the type of procedure wherein it originated, and it is therefore a suggestive analogy for other trusteeships, particularly in the field of real estate securities." (*Report on the Study and Investigation of Reorganization Committees*, Part VI, p. 185.)

The Bureau of Trust Supervision

With the termination of the Mortgage Commission and the trusteeing of almost all of the certificated mortgages, the judges assigned to this work became vested with the responsibility of supervising the operation of the liquidating trusts. The Schackno and Mortgage Commission Acts had fully served their purpose in accomplishing reorganizations of the issues. In order to continue the supervision of the issues, a currently operating method had to be established. By Chapter 704 of the Laws of 1940, the Legislature authorized the courts to appoint, and at pleasure remove, one or more competent persons to examine into all matters relative to these trusts. Pursuant to this statute, Mr. Justice Brower created the Bureau of Trust Supervision to assist him in the supervision of the trust estates within his jurisdiction.

There will be provided for the Court upon argument copies of the Report of the Bureau of Trust Supervision, which is on file in the Office of the County Clerk of the County of Kings (file No. 5791/1940). This report sets forth with particularity the method of operation of that

Bureau. We submit that this report amply demonstrates that the State of New York, through its judicial branch, is affording to the certificate holder creditors a high measure of protection, and that the interests of these creditors can be best subserved in continuing the present method of supervision in the State Courts.

The Report of the Bureau of Trust Supervision clearly demonstrates that it is well equipped as an agency for the protection of creditors. Its personnel is experienced, and competently trained to handle the problems. The Bureau has the advantage of close cooperation with the State agencies which have heretofore administered these issues. More important, there is the necessary continuity in the administration of the properties. There is more to the proper administration of mortgages and real estate than appears on first examination. The past history of the properties is most important. All of the information compiled over the past ten years on each of the properties is available to help the Bureau reach a conclusion as to the most advisable method of reorganization.

The main functions of the Bureau of Trust Supervision fall into two principal categories: (1) the examination and audit of the annual and final accountings rendered by trustees and the making of reports in connection therewith; (2) the examination and analysis of applications by trustees, owners, certificate holders and other interested parties relative to the sale of real property, liquidation and extension of bonds and mortgages and miscellaneous applications for instructions and the making of reports to the Court relative thereto.

Another very important function is the direct service that it renders to certificate holders, of whom there are more than 150,000 holding investments in mortgages, in the Court in which this Bureau functions. The certificate holders have the advantage of having an agency to which they may go for information and advice, without charge to them.

We briefly summarize the volume of work which passes through this Bureau: During the period from May 10, 1940 to June 30, 1942, there was considered by the Kings County Supreme Court and examined and reported on by the Bureau, a total of 1,986 motions or applications by trustees, property owners, certificate holders and other interested parties, exclusive of accounting matters. These 1,986 motions or applications involved an aggregate principal face amount of mortgages of $159,016,648.* It was necessary for the Bureau to make 3,201 appearances in court on these matters. The average number of such transactions is in excess of seventy-six per month. This work is constant, because of the provisions of the Trust Declarations which require Court approval of the important steps taken under these plans.

We respectfully invite attention to that part of the Bureau's report (p. 18) which shows a liquidation of collateral of the principal amount of $44,529,617.85 up to December 31, 1941, and to that part which shows that as of December 31, 1941 there were 5,084 mortgages totalling a principal amount of $197,827,559.73 in good standing, and 477 mortgages in principal amount of $14,319,519.46 in default. It also appears that during the calendar year of 1941, trustees made distribution to investors of $18,811,065.27 on account of principal and interest.

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*While the bulk of these motions was naturally made by the trustees, there were a number of applications made by other parties in interest and reported on by the Bureau and passed upon by the Court. For instance, there were twenty-four motions by owners of mortgaged real estate for varying relief such as modifications of plans, reargu-ments, etc., as well as several motions by prospective purchasers of real property to procure approval of offers to purchase, and by certificate holders to compel trustees to take action on proposals submitted to them,—all of which were determined by the Court on the merits. It may also be noted that during this period there were several appeals to the Appellate Division by owners of mortgaged premises, some of which resulted in reversals and some in affirmances. This is particularly relevant in view of the claim made below that the debtor had no voice in the State Court proceedings.

The total cost of operating the Bureau for the period from May 10, 1940 to June 30, 1942 amounted to $69,554.92, or an average of $32,519.36 per year, or .011614 of one percent per annum of the estimated average principal amount of the mortgages under the jurisdiction of the Court during that period.

We respectfully submit that in dealing with a tremendous local problem of this nature it is highly advantageous that an agency such as the Bureau of Trust Supervision should be geographically located where the problem exists. There are many other facts contained in the report of the Bureau which demonstrate the extent of its work and the efficiency with which it is done. We believe that the Bureau of Trust Supervision is an agency which is fully competent to afford to the public all of the protection that can possibly be rendered by any agency, including the Securities and Exchange Commission. All of the powers which the Securities and Exchange Commission claims that it has, are here present in a larger degree. The Commission's contention that no adequate measures exist in the State Court to protect the rights of the parties to these proceedings, fails in these statutory and purely local proceedings where a comprehensive program for the complete and inexpensive protection of mortgage investors has been established.

Administration of these liquidating trusts should be left with the State Supreme Court to be administered with the advice and guidance of the Bureau of Trust Supervision and of the other agencies and trained personnel in other departments.

We have placed emphasis upon the protective devices taken by the Supreme Court in the Second Judicial Department because that is the Department out of which this litigation arises. Other Departments having to do with these problems have taken equally adequate measures, by means of trained personnel, to protect the interests of the public.

State Court Proceedings versus Chapter X Proceedings

We are mindful of the fact that Chapter X states that for a petition to be dismissed, it must be shown that the interest of creditors would *best* be subserved in the prior proceeding and that, therefore, it may be argued that it is not sufficient to show that the State Court proceedings are fully adequate in themselves. The statute is such that the argument might be made that it must appear, *after comparison*, that the State proceeding is best for creditors.

In the first place, the burden of showing that the State proceeding will *not* best subserve creditors' interests is on the petitioner—not respondent (see Respondent's Brief, pp. 9-10).

We further contend that in a case such as the instant one, in which the debtor has no assets other than a piece of mortgaged real estate, wherein the amount of the mortgage is in excess of the appraised value of the real estate (Record, pp. 17-20) and where the local problem involved is one which has been described by the Securities and Exchange Commission as of "unique complexity and peculiar difficulty" (Securities and Exchange Report, Vol. VI, p. 185), a comparison of the State and Federal proceedings will indicate that the State proceeding will best serve those interests.

The situation as it exists in this case is by far the most common situation in the reorganization of certificated mortgages in New York. All of the certificated mortgages were placed upon the properties involved prior to February, 1933, at a time when higher real estate values existed and, in turn, larger mortgages were the rule and not the exception. Such properties were almost invariably the only asset of the corporate owner. With the deflation of the value of real estate to lower levels, it followed that in very many cases the amount of the certificated mortgage was found to be in excess of the true value of the property it encumbered.

There has been little or no experience of reorganization of certificated mortgages under Chapter X, whereas under

the State Court procedure, any analysis of its desirability can be implemented by the experience of some nine years of work (see *Bureau of Trust Supervision's Report*). An analysis of Chapter X for this purpose must be limited to the Act itself. Although a lack of experience is not necessarily controlling, it should be a very weighty factor in a field as complex and peculiarly local as this one.

The State of New York has recognized its responsibilities to the hundreds of thousands of holders of certificates, has invested large sums of money for the creation of agencies to protect them, and through these expenditures has trained competent personnel who are familiar with the history of the mortgages involved and with the details of the problems presented. This personnel continues to exercise supervision for the benefit of certificate holders through the Bureau of Trust Supervision in Kings County and through other personnel in other counties. The judges, such as Judge Brower in Kings County, have had years of experience with these mortgages. Complete files running from the inception of the mortgages, taken from the files of the guaranty companies, running on through the period of supervision by the Superintendent of Insurance through the period of supervision by the Mortgage Commission and now into the period of supervision by the Bureau of Trust Supervision, are available to the Bureau and to the courts. We fail to see how anything but disadvantage can result from upsetting this smooth-working mechanism and transferring these mortgages to the jurisdiction of the Federal Court.

In those instances in which the Securities and Exchange Commission would be made a party, its personnel would not necessarily be trained in mortgage or real estate problems.* Their experience is with security issues and large

* The Securities and Exchange Commission must be made a party only in those proceedings wherein three million dollars or more are involved (11 U. S. C., Sec. 572). There are no certificated mortgages involved in Schackno proceedings whose amounts total three million dollars.

industrial corporations. While it has been argued that disinterested trustees would be appointed in many instances, it must be remembered that Chapter X only provides for disinterested trustees when the principal amount of the mortgage exceeds $250,000. (11 U. S. C., Sec. 556.)

An examination of the files shows that at least 75% of Schackno mortgages are less than $250,000 in principal amount. The result would be that either the debtor itself would remain in control under Chapter X to the decided detriment of certificate holders, or a trustee would be appointed. After that individual was appointed trustee, he would have to formulate a plan of reorganization which would necessarily follow one of two alternative courses: first, the formation of a corporation in which certificate holders would become stockholders and which would take title to the property, or second, the sale of the property to an outsider. The disadvantage of the corporate form of reorganization and the arguments in that respect are set forth fully in the trustee's brief, pages 23-24.

See also:

In re Lawyers Westchester Mortgage & Title Co., Sup. Ct., Westchester Co., N. Y. Law Journal, Feb. 7, 1934;

In re N. Y. Title & Mortgage Co., 153 Misc. 838.

If the alternative of sale were adopted, the individual trustee appointed in the Federal Court would not necessarily effectuate a sale of the property as advantageously as would the corporate trustee, who had previously administered the property in question and who was familiar with its history. Moreover, any such plan would not have the advantage of examination by the State Court, which has all of the records and history of the particular property and of similar properties, available to guide it in passing upon the fairness or desirability of the plan; nor would it be subject to the recommendation of the Bureau of Trust Supervision, which has similar records and experience.

In addition, as pointed out in the trustee's brief (pp. 27-31), the expense of a Chapter X proceeding is prohibitive in comparison with the expense of the reorganizations in the trust proceedings in the State Court. See, *In re Castle Beach Apartments, Inc.*, 135 F. (2d) 762; *In re Frank Realty Co.*, 31 Fed. Supp. 816.

Other mechanical difficulties would arise in the Federal Courts. In a group issues (see *Paloma Estate* case, action in *certiorari* held in abeyance May 12, 1942), where there are more than 100 mortgages and properties and more than 7,500 certificate holders, under Chapter X the 7,500 certificate holders would have to be parties to the proceeding with the attendant enormous expense of several printings and mailings. The remainder of the mortgages would nevertheless still be subject to the jurisdiction of the State Court and its trustee with needless confusion, duplication and overlapping of effort.

Both the District and Circuit Court Justices in the Southern District and Second Circuit, respectively, have recognized these problems and have permitted the administration of Schackno mortgages to remain in the State Courts.

Jacoby v. *Bond & Mortgage Guarantee Co.*, 72 F. (2d) 420, cert. den. 293 U. S. 619;
Tolfree v. *New York Title & Mortgage Co.*, 72 F. (2d) 702, cert. den. 293 U. S. 619;
Depew v. *Lawyers Title & Guaranty Company*, 72 F. (2d) 705, cert. den. 293 U. S. 619;
Brooklyn Trust Co. v. *Rembaugh*, 110 F. (2d) 838;
In re Paloma Estates, Inc., decided Feb. 21, 1942 (Judges Learned Hand, Chase and Clark) unreported;
In re Blinrig Realty Corp., 114 F. (2d) 100.

See also:

Francfair, Inc., 13 F. Supp. 513 (S. D. N. Y.);
In re Reliable Estates, 33 F. Supp. 588 (E. D. N. Y.);
In re Coney Island Hotel Corp., 76 F. (2d) 126.

We, therefore, see no reason why these Schackno trusts should be terminated in the State Court and brought into the Federal Court. If that is done, ten years of progress by New York State in the solution of these difficult problems will be seriously impeded, to the detriment of the certificate holders, practically all of whom are citizens of this State. We agree with Mr. Justice Douglas who said, when discussing state control in wage earner bankruptcies:

> "It seems desirable * * * to utilize to the fullest possible extent the administrative procedures and techniques which states have evolved or with which they have gained experience. The alternative of raising a new and huge federal superstructure to handle a function of some familiarity and experience in the states seems unwise" (42 Yale Law Journal 637).

See also:

Pennsylvania v. *Williams*, 294 U. S. 176.

We, therefore, respectfully submit that the order of the United States Circuit Court of Appeals should be affirmed.

Respectfully submitted,

JOHN J. BENNETT, JR.,
Attorney General of the State of New York, for the People of the State of New York.

HENRY EPSTEIN,
Solicitor General.

JOHN F. X. MCGOHEY,
Assistant Attorney General.

EDWARD F. KEENAN,
General Counsel, Superintendent of Insurance.

BENJAMIN HEFFNER,
Assistant Attorney General,
of Counsel.

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CHARLES ELMORE CROPLEY
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1942.

MARINE HARBOR PROPERTIES, INC.,
Petitioner,

AGAINST

MANUFACTURERS' TRUST COMPANY, *et al.*,
Respondents.

No. 24.

Petition to Have This Honorable Court Reconsider Its Decision Herein and Upon Such Reconsideration Order That This Case Be Remanded to the District Court Where the Debtor May Amend Its Petition to Allege and Prove a Proper Case in Accordance With the Opinion of This Honorable Court, or in the Alternative, That the Mandate of This Court and the Order to Be Entered Thereon Be So Worded As to Provide an Opportunity to the Debtor to File An Amended Petition for Reorganization in the District Court, and That the Costs Herein Be Allowed to Abide the Event.

To the Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

The petition of Marine Harbor Properties, Inc., hereinafter called the debtor, respectfully shows:

On September 17, 1941, the debtor filed a petition for reorganization under Chapter X of the Bankruptcy Act. This petition was approved by an *ex parte* order entered in the District Court. No answer to such petition has ever been filed.

Shortly thereafter, the predecessor-in-interest of the Manufacturers' Trust Company, the present respondent, moved to vacate this *ex parte* order, based upon affidavit proof only. This motion was opposed by the debtor, but again, on affidavit proof only. On this proof, the respondent's motion was denied. The District Court found that, in its opinion, the debtor had shown good faith and sufficient need for relief under Chapter X.

An appeal was taken to the Circuit Court of Appeals where the decision of the District Court was reversed on the authority of that Circuit Court's previous holding in *Brooklyn Trust Company* v. *Rembaugh*, 110 Fed. (2) 838.

In the appeal to this Court, the *Rembaugh* case, *supra*, was distinctly disapproved, but affirmance of the decision of the Circuit Court was nevertheless had for the reason that, in the opinion of this honorable Court, the debtor had insufficiently shown its good faith and need for relief. Only in this Court, and here for the first time, was it pointed out wherein and why the debtor had failed to make a sufficient showing on these two issues.

A mandate is to be issued out of this Court in accordance with its opinion and an order is to be entered thereon. It is expected that in accordance with this opinion, the petition of the debtor will be dismissed.

Petitioner respectfully states that the insufficiency of its showing in the District Court on the issues of good faith and need for relief was not the result of carelessness, neglect, or some ulterior motive. The insufficiency was due solely to the fact that this honorable Court had not yet indicated in this, or any other case, the extent and

nature of the burden which debtors must discharge on the issues of good faith and need for relief. Both the District Court and the Circuit Court of Appeals were unable to point out wherein and why the debtor's petition for reorganization was insufficient because of the silence of the law on this subject. Now, however, in the light that has been shed on this subject through the decision and opinion of this Court, it is to be expected that the lower Courts as well as debtors petitioning for reorganization will be better guided.

In the event, however, that the debtor's petition herein is dismissed, as is to be presumed from the decision of this Court, it would necessarily bar the debtor from ever reorganizing in the Federal Court, even though it can sufficiently demonstrate its good faith and need for relief. This would unduly penalize the debtor, especially because the debtor presently possesses knowledge of specific facts which it believes will clearly indicate to the Court its good faith and need for relief under Chapter X. The debtor believes it can show wherein and why none of the prior proceedings will best subserve the interests of creditors or stockholders. The debtor also believes that it can make a sufficient showing that the necessary contribution it may be required to make to the interests of creditors is based on solid fact and not mere hope.

Until now, however, there has been no opportunity to have in the District Court a direct and fair test of these issues in accordance with the opinion of this honorable Court. The previous attack on the debtor's petition, as the history of this case indicates, was based upon and sustained by the Circuit Court's holding in the *Rembaugh* case, *supra*. Since the rationale of the *Rembaugh* case has been disapproved here, and neither the District Court, nor the debtor had the benefit of the opinion of this hon-

orable Court by which to be guided on the issues of good faith and need for relief, the debtor feels justified in asking this Court for an opportunity to amend its petition, so that it may allege and prove a proper case.

This opportunity is desired because the debtor feels it can demonstrate that in many ways, the prior proceedings, both the foreclosure and Schackno, withhold from and/or deny to creditors or stockholders the benefits, advantages or protections which Chapter X affords. When these allegations are adequately explained and a full hearing has been had thereon, it will clearly indicate that reorganization of the debtor cannot possibly be effected in any other Court or proceeding except in the Federal Court and under Chapter X.

The necessary contribution which the debtor may be called upon to make in accordance with the principles of this Court as laid down in *Case* v. *Los Angeles Lumber Products Co.*, 308 U. S. 106, is available. The present stockholders are also the sole stockholders in other corporations whose equities are substantial. These equities will, if necessary, be pledged, assigned or transferred in such manner as the Court may require to insure to creditors that a contribution will be forthcoming from the debtor whenever a plan of reorganization has been adopted that is fair, equitable, and feasible.

WHEREFORE, the debtor respectfully prays that this honorable Court reconsider its decision herein, and upon such reconsideration, order that this case be remanded to the District Court where the debtor may amend its petition to allege and prove a proper case in accordance with the opinion of this honorable Court, or in the alternative that the mandate of this Court and the order to be entered thereon be so worded as to provide an oppor-

tunity to the debtor to file an amended petition for reorganization in the District Court and that the costs herein be allowed to abide the event.

Dated, November 30, 1942.

FRIEDLAND & FRIEDLAND,
Counsel for Petitioner,
Marine Harbor Properties, Inc.

STATE OF NEW YORK,
COUNTY OF NEW YORK. } ss.:

SOL FRIEDLAND and ARTHUR E. FRIEDLAND, being duly sworn, depose and say, that they are counsel for the petitioner named in the foregoing petition. That they prepared the same and that the allegations thereof are true as they thoroughly believe.

SOL FRIEDLAND,
ARTHUR E. FRIEDLAND.

Subscribed and sworn to before me
this 30th day of November, 1942.

SYLVIA LICHTENSTEIN,
Commissioner of Deeds,
New York City.
N. Y. County Clerk's #157.
Commission Expires December 23, 1943.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1942

MARINE HARBOR PROPERTIES, INC.,
Petitioner,
against
MANUFACTURERS TRUST COMPANY, *et al.*,
Respondents.

No. 24

ANSWER TO PETITION FOR "RECONSIDERATION"

Petitioner, Marine Harbor Properties, Inc., seeks to have this Court so "reconsider its decision herein" and so issue its mandate as to permit petitioner in the district court to amend its petition under Chapter X. It also requests that "the cost herein be allowed to abide the event". The petition, verified only on "belief" by counsel, is not supported by a certificate of counsel which meets the requirements of Rule 33 of the rules of this Court.

The petition appears to be a mere endeavor to prolong a case which has already been argued in three courts over a fourteen-month period.

Petitioner's chief contention that, until the announcement of this Court's opinion, it was not sufficiently warned of the required contents of a petition under Chapter X in the circumstances of this case, is wholly without merit. Throughout the proceeding this respondent's major contentions were that the tests of Section 146(3) and (4) had not been satisfied. The fact that the Circuit Court of

Appeals grounded its decision in large part upon the rule of *Brooklyn Trust Company* v. *Rembaugh*, 110 F. (2d) 838, which this Court's opinion disapproved, in no way affected the issues under that section. The questions of which petitioner now seeks reconsideration are the very ones which have been thoroughly litigated throughout the proceeding.

Thus, it argues that it should be permitted to amend its Chapter X petition because it "believes it can show wherein and why none of the prior proceedings will best subserve the interests of creditors or stockholders", and that "this opportunity [to amend] is desired because the debtor feels it can demonstrate that in many ways, the prior proceedings, both the foreclosure and Schackno, withhold from and/or deny to creditors or stockholders the benefits, advantages or protections which Chapter X affords." But that was the issue under Section 146(4), which was thoroughly argued in all courts and upon its decision on which this Court's opinion was based.

Again, the petition for reconsideration states that the debtor "believes that it can make a sufficient showing that the necessary contribution it may be required to make to the interests of creditors is based on solid fact and not mere hope". Similar statements were made upon the argument of the case in this Court and in the Circuit Court of Appeals. This Court in its opinion commented on the absence of any evidence that the rule of *Case* v. *Los Angeles Lumber Products Co.*, 308 U. S. 106, could be complied with here.

The suggestion in the petition, that "equities" in other corporations owned by petitioner's stockholders "will, if

necessary, be pledged * * * to insure to creditors that a contribution will be forthcoming from the debtor whenever a plan of reorganization has been adopted that is fair, equitable, and feasible", disregarding its equivocal character, is at best only a suggestion that petitioner should be afforded further opportunity to attempt to make its petition square with the principles of *Case* v. *Los Angeles Lumber Products Co.* But the doctrine of "absolute prorities" applied in that case was the established law when the debtor filed its petition under Chapter X.

The substantial deficiency in the first mortgage alone is shown in the record (R. 15, 17, 56-57, 60, 71). In addition there is a second mortgage of $25,000 (R. 82). We submit therefore that it will serve no purpose to permit further proceedings by the debtor predicated on a mere possibility of a pledge of "equities". It is doubtful that even the court costs of this litigation can be recovered from the debtor, which is concededly insolvent and has no assets other than the mortgaged property. Certificate holders have had to carry a heavy burden in contesting the Chapter X proceeding. We submit that the instant application is merely an endeavor to preserve for the 'equity owners a wholly unjustified nuisance value' (see opinion of this Court, p. 5).

Certificate holders should not be further delayed in their efforts to reduce their security to possession. If the petitioner were acting in good faith, it could at any time during the foreclosure litigation (as indeed it still can) tender the amount of the defaults, other than principal, on the first mortgage, and in that event the mortgage foreclosure proceeding in the state court would be automatically terminated (*New York Civil Practice Act, Section 1077-e*).

We submit that the petition for "reconsideration" should be in all respects denied and that the mandate of this Court should unconditionally require the affirmance of the order of the Circuit Court of Appeals dismissing the debtor's petition.

Respectfully submitted,

CHARLES E. HUGHES, JR.,
CURTISS E. FRANK,
Counsel for Respondent
Manufacturers Trust Company,
As Trustee.

December 3, 1942.

SUPREME COURT OF THE UNITED STATES.

No. 24.—October Term, 1942.

Marine Harbor Properties, Inc., Petitioner, *vs.* Manufacturer's Trust Company (Successor by Merger to the Mortgage Corporation of New York), as Trustee, etc., et al.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

[November 9, 1942.]

Mr. Justice Douglas delivered the opinion of the Court.

The question in this case is whether the Circuit Court of Appeals was in error in holding that a debtor's petition filed by petitioner under Ch. X of the Bankruptcy Act (52 Stat. 883, 11 U. S. C. § 501) was not filed in "good faith".

The debtor's sole asset is an apartment building in New York City which is subject to a first mortgage of $370,000. This mortgage is held by the respondent, Manufacturer's Trust Co. (successor to The Mortgage Corporation of New York) as trustee for certificate holders. There are also junior mortgages and other claims, including an unspecified amount of unsecured indebtedness. Concededly the property of the debtor is worth less than the amount of the first mortgage debt. The first mortgage was originally created in 1931 and was held by Title Guarantee and Trust Co. which issued and sold to the public certificates of participation, guaranteed as to principal and interest by Bond and Mortgage Guarantee Co. The latter company became involved in financial difficulties in 1933 and was taken over by the Superintendent of Insurance of New York for rehabilitation.[1] Pursuant to provisions of the Schackno Act (N. Y. Laws 1933, c. 745) the Superintendent of Insurance promulgated in 1934 a plan for the readjustment of the rights of the certificate holders in the mortgage by which the mortgage was extended to December 1, 1937 and the interest reduced. Over two-thirds of the certificate holders con-

[1] See generally, Report of Commissioner George W. Alger to the Governor of the State of New York, Oct. 5, 1934.

sented to the plan and the debtor joined in the extension agreement. The New York court approved it. In 1935 the New York Mortgage Commission succeeded the Superintendent of Insurance as administrator of certificated bonds and mortgages. N. Y. Laws 1935, c. 19, c. 290. That Commission[2] in 1938 proposed the designation of the Mortgage Corporation of New York as trustee of the bond and mortgage in the instant case under a declaration of trust granting the trustee broad and comprehensive powers. This proposal was consented to by over two-thirds of the certificate holders and approved by the New York court. The order of the court provided "that this Court, having assumed jurisdiction of this proceeding, shall retain jurisdiction hereof until the complete liquidation of the Trust Estate and the termination of the trust; and the Trustee, or any other interested party herein, may apply at the foot of this Final Order upon such notice as the Court may direct for such other and further relief as to the Court may seem just and proper."

The principal of the first mortgage was not paid at its extended maturity in 1937. But until April 1, 1941, the debtor made all other payments due under the 1934 extension agreement. At that time the debtor defaulted in payment of interest and taxes. Both before and after that default the debtor and the trustee negotiated for an agreement of further extension and modification. But no agreement between them could be reached and no further proposal for a modification or extension of the mortgage was presented to the state court or to the certificate holders. On May 1, 1941, the trustee instituted foreclosure proceedings in the state court. A receiver was appointed who took possession. In September 1941 the debtor filed its voluntary petition under Ch. X of the Bankruptcy Act. An *ex parte* order approving the petition and appointing trustees was obtained. Shortly thereafter the mortgage trustee moved to vacate that order and to dismiss the debtor's petition on the ground that it was not filed in "good faith". That motion was denied. 41 F. Supp. 814. The Circuit Court of Appeals reversed, one judge dissenting. 125 F. 2d 296. We granted the petition for certiorari because of the importance in the administration of the Bankruptcy Act of the problems involved.

Every petition under Ch. X must state, *inter alia*, "the specific facts showing the need for relief under this chapter." § 130(7).

[2] On the activities of the Commission see Annual Report 1939, N. Y. Leg. Doc., No. 94.

Sec. 141 provides that the judge shall enter an order approving a debtor's petition "if satisfied that it complies with the requirements of this chapter and has been filed in good faith, or dismissing it if not so satisfied." Sec. 146 defines "good faith" and provides in part:

"Without limiting the generality of the meaning of the term 'good faith', a petition shall be deemed not to be filed in good faith if—

. . . . . .

"(4) a prior proceeding is pending in any court and it appears that the interests of creditors and stockholders would be best subserved in such prior proceeding."

The federal bankruptcy power is, of course, paramount and supreme and may be so exercised by Congress as to exclude every competing or conflicting proceeding in state or federal tribunals. *Kalb* v. *Feuerstein*, 308 U. S. 433. In fashioning Ch. X Congress, however, did not go so far. While the pendency of prior proceedings in state or federal courts does not bar the filing of a petition under Ch. X (§ 256), Congress in effect directed the bankruptcy courts not to approve petitions under Ch. X in such cases unless it appeared that the interests of creditors and stockholders would not be best subserved in the prior proceedings. And it put the burden on the petitioner to make that showing. The report of the House Judiciary Committee states that the purpose of § 146(4) was to "stop the removal of prior pending cases from other courts where the interests of creditors and stockholders would be better served by retaining and continuing the prior proceedings." H. Rep. No. 1409, 75th Cong., 1st Sess., p. 42. Sec. 146 represents a codification of some of the interpretations which the courts had given the words "good faith" in proceedings under § 77B. S. Rep. No. 1916, 75th Cong., 3d Sess., p. 27. Thus the necessity of showing "a need for the machinery of 77B as an essential in accomplishing a reorganization because other procedures were either unavailable or more cumbersome and expensive" led courts to find an absence of "good faith" in the sense that no "need for relief" had been established, where 77B was sought to be employed by a debtor as "a mechanism for preserving equities at the expense of creditors." See Report on the Study and Investigation of the Work, Activities, Personnel and Functions of Protective and Reorganization Committees, Securities and Exchange Commission, Pt. VIII, p. 94 (1940).

In view of that history it seems clear that when a prior proceeding is pending, a petitioner's showing of "need for relief" under Ch. X, required to be contained in every petition by the express provisions of § 130(7), must demonstrate that at least in some substantial particular the prior proceedings withhold or deny creditors or stockholders benefits, advantages, or protection which Ch. X affords. In absence of such a showing the "need for relief" has not been established and the District Court is not enabled to make an informed judgment on the "good faith" issue.

The Circuit Court of Appeals in this case, as in *Brooklyn Trust Co.* v. *Rembaugh*, 110 F. 2d 838, held that the debtor's petition was not filed in "good faith" since it was seeking to escape the jurisdiction of the state court to which it had voluntarily submitted itself. But that is not the test which Congress has provided in § 146(4). That provision requires the bankruptcy court to inquire whether "the interests of creditors and stockholders" would be better subserved in the prior proceedings or under Ch. X. That the desire of the petitioner to escape the prior proceedings is immaterial to that inquiry is supported not only by the language of § 146(4) but also by the fact that § 256 expressly sanctions the filing of petitions under Ch. X although prior proceedings are pending. To disqualify a petitioner under Ch. X merely because he had in some way participated in the prior proceeding would effect a substantial impairment of § 146(4), since it would be the exception rather than the rule where both the debtor and the creditors had not taken some part in the prior proceedings. Furthermore, the issue as to the adequacy of the prior proceedings as compared with Ch. X is the same whether the petition is filed by creditors or by the debtor. All petitions whether filed by the debtor or by others must show the "need for relief" (§§ 130-131); and in every case the bankruptcy court must be satisfied that the petition has been filed in "good faith". §§ 141-144.

We are of the opinion, however, that the debtor did not sustain the burden which the federal statute places on a petitioner. So far as the "interests" of stockholders are concerned it is not apparent that the equity owners would be denied in the state foreclosure proceedings benefits, advantages, or protection which Ch. X would afford them. Admittedly the property is worth less than the amount of the first mortgage indebtedness. Under the

rule of *Northern Pacific Ry. Co.* v. *Boyd*, 228 U. S. 482, and *Case* v. *Los Angeles Lumber Products Co.*, 308 U. S. 106, a plan of reorganization would not be fair and equitable which in such circumstances admitted the stockholders to participation, unless the stockholders made a fresh contribution in money or in money's worth in return for "a participation reasonably equivalent to their contribution." *Case* v. *Los Angeles Lumber Products Co., supra*, p. 121. That rule obtains under Ch. X as well as under its predecessor, § 77B. There is no suggestion in the record that the equity owners desire to make a contribution on that basis and that unless they are allowed to do it under Ch. X, they will be barred. All that the record shows is an affidavit by one Silverman that "if the creditors desire liquidation of their claims on the basis of present actual values rather than on the face amount of their claims", $50,000 in cash could be raised. Ch. X would not permit such a dilution of creditors' interests. Hence such a showing does not establish on behalf of the stockholders that "need for relief", which § 130(7) read in light of § 146(4) requires. In fact, the approval of the petition on that ground would be giving the equity owners a nuisance value wholly unjustified by the reorganization standards which are incorporated into Ch. X.

The District Court, however, concluded that it was in the interests of all the creditors that the Ch. X petition be approved. It noted that the market value of the certificates was far under par and that there were lienors and creditors other than the first mortgage certificate holders with which the bankruptcy court, but not the state court, could deal. If there were a showing, for example, that the property was worth more than the amount of first mortgage indebtedness and it appeared that that excess value would be lost to the junior interests in the state proceedings or that the state proceedings were less adequate by reorganization standards than the bankruptcy court to protect such interests, approval of the petition clearly would be justified whether filed by the debtor or by creditors. But no such showing was made. Hence it was not established that continuation of the state proceedings would deny the junior creditors any benefits which Ch. X would afford them. Approval of the petition on the grounds advanced by the District Court could be made only under the composition theory of reorganization which Ch. X, like § 77B, rejected in favor of the full priority rule of the *Boyd* case. See

Case v. *Los Angeles Lumber Products Co., supra*, p. 119, nt. 14. That rule protects the rights of senior creditors against dilution either by junior creditors or by equity interests. See *id., p.* 123; *Consolidated Rock Products Co.* v. *Du Bois*, 312 U. S. 510, 525-526, 529-530.

There remains the contention that it was in the "interests" of the certificate holders to have the proceedings transferred to Ch. X. In this connection much emphasis is placed on numerous safeguards contained in Ch. X which this Court reviewed in *Securities and Exchange Commission* v. *United States Realty & Imp. Co.*, 310 U. S. 434, 448-450. And it is asserted that comparable safeguards are wholly or largely lacking in proceedings under the Schackno Act. Those considerations would be highly relevant and persuasive if this was a case of the usual reorganization proceeding dealing with more than one class of securities under the older procedures which Ch. X was designed to improve and supplant. See *Securities and Exchange Commission* v. *United States Realty & Imp. Co., supra*, p. 448; H. Rep. No. 1409, 75th Cong., 1st Sess., pp. 37 *et seq.* Then the safeguards afforded by Ch. X would have special significance in protecting the respective classes of investors against improvident, unfair or inequitable adjustments, compromises, and settlements, steps which are basic to the reorganization process but which in selfish hands led to much abuse. H. Rep. No. 1409, 75th Cong., 1st Sess., pp. 37 *et seq.* But here the machinery of the state which is being used is the foreclosure proceeding which so far as appears has been invoked on behalf of the certificate holders alone. Presumptively, the result of the foreclosure will be an appropriation of the assets of the debtor for the benefit of the certificate holders exclusively. There is no showing that the foreclosure proceedings have been conducted in such a way as to jeopardize the interests of the certificate holders contrary to the design of Ch. X. There is no showing that assets subject to the payment of the certificates are being neglected. Thus it is not shown that the claim against the guarantee company is not being pursued or that its collection could better be handled in proceedings under Ch. X. There is no showing that the machinery employed or available in the state foreclosure proceeding to safeguard and protect the interests of those creditors *after* the sale is not comparable to that contained in Ch. X for the consummation of plans which are not only fair

but feasible. § 221(2). In view of the burden on a petitioner to make the showing required by § 130(7) and § 146(4), the bankruptcy court is not warranted in assuming without more that a state foreclosure proceeding instituted for and on behalf of the first mortgage creditors exclusively is inadequate, measured by Ch. X standards, to protect their interests. The contrary course would result in Ch. X making greater inroads on prior proceedings than § 130(7) and § 146(4) indicate was the purpose.

Affirmed.

A true copy.

Test:

Clerk, Supreme Court, U. S.